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CONCENTRATION OF MARKET POWER, through mergers, take-overs, joint ventures and other acquisitions of control, AND ITS EFFECTS ON INTERNATIONAL MARKETS, in particular the markets of developing countries

Revised report by the UNCTAD secretariat

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SUMMARY AND CONCLUSIONS

A. Acquisitions of control - trends and effects

(i) There has been a massive increase in mergers in developed countries during the 1980s. Although it has undergone a relative decline in some countries during the last four years, merger activity looks likely to continue at a high rate in the 1990s. Joint ventures and cross-shareholdings among companies have also greatly increased. Merger activity in developing countries has been relatively small, but the growth rate has been significant, particularly in Latin America and, to a lesser extent, in the Far Eastern region. The structures of the industries, capital markets and firm organization in most developing countries have hitherto tended to impede mergers, but an evolution is taking place. Joint ventures between firms from developed and developing countries are far more common than mergers. Privatization is also taking place on a large scale in many countries. The growth in these different types of acquisitions of control has been influenced, *inter alia*, by the globalization of markets, the greater intensity of competition, the need to share costs and risks, and the universal trend towards liberalization and deregulation.

(ii) It is impossible to generalize about the effects of mergers and joint ventures upon the markets of developing countries; a case-by-case analysis is necessary. Mergers and joint ventures among locally established firms are likely to have a strong impact on the markets of developing countries because these are usually highly concentrated. Low demand in these markets can sustain relatively few firms producing on a minimum economic scale, while other obstacles to new market entry include limited availability of entrepreneurship and production inputs, inefficient distribution and communications systems, poor information flows and regulatory barriers. This would suggest a need for greater awareness regarding both possible anti-competitive effects of mergers and joint ventures and opportunities they may provide for new market entry or stronger competition against market dominant firms. It would also be necessary to take into account that mergers and joint ventures may lead to either less or greater micro- and macro-economic efficiency in respect of investment, management, production, sales or technological innovation. While they may also reduce the healthy stimulus to efficiency provided by competitive markets, higher market concentration may not necessarily lead to reduced competition or efficiency.

(iii) In the specific context of developing countries, a cost-benefit analysis of acquisitions of control may particularly need to take into account such considerations as high market concentration, low resource supply and market demand, the importance of economies of scale and scope and the relative efficiency of vertical integration or outsourcing in the relevant industries, and the international competitiveness of such industries. Acquisitions of control among local firms may improve their competitiveness vis-à-vis foreign competition, but it should not be assumed that such acquisitions will necessarily improve competitiveness. Conversely, market entry by foreign investors or by imports may diminish concerns about anti-competitive effects arising from acquisitions of control because it would increase competition, even though foreign competition may, in some cases, strengthen market concentration by leading to market exit by some local firms. However, foreign competition is often not a perfect substitute for local competition, especially in developing country markets, because of barriers to entry into such markets and because of other factors, such as product market segmentation, discriminatory price policies by transnational corporations (TNCs), and lack of foreign exchange for imports (this latter factor suggests a link between developing country exports and competition in their domestic markets). Premature exposure to foreign competition may also, by decimating infant industries, lead to the replacement of a local oligopoly by foreign oligopoly. The existence of effective competition in developing countries' markets would be necessary for foreign competition to fully realize its potential for strengthening compe-

tition in these markets.

(iv) Mergers or joint ventures between local firms and established TNC subsidiaries or between TNC subsidiaries do not raise issues relating to market concentration that are different in principle. Where the TNC concerned is entering *de novo* a developing country, this may, depending upon the circumstances, provide a healthy competitive stimulus to concentrated markets. In terms of efficiency, acquisitions of control between TNCs and local firms raise much the same issues as greenfield investment by a TNC in terms of finance, management efficiency, technology transfer, imports and exports but, depending upon the circumstances, there may be additional advantages or disadvantages in one or other form of investment.

(v) Some mergers and joint ventures occurring in developed countries have affected developing country markets through restrictions on the freedom of affiliated firms to compete, and by heightening possibilities for international collusion and cartelization in a number of industries, although such possibilities may have yet to be fully realized. In addition to such industries, overseas mergers would particularly affect developing countries where they occur among trading intermediaries; in some agricultural commodity sectors such as processed tea, coffee or cocoa; in some service sectors; and in high-technology areas such as the biotechnology, computer or semiconductor industries. Although competition does take place among oligopolists in such product markets, it does not necessarily extend to all geographical markets, or necessarily take the form of price competition. However, overseas mergers and joint ventures have also resulted in positive effects for developing countries. They have helped some foreign firms to compete better against other market-dominant firms trading with developing countries, as well as leading to increased investment in individual developing countries. Both trade and foreign investment liberalisation should magnify the effects of overseas acquisitions of control upon developing countries.

B. Policies and cooperation

(vi) An integrated approach is necessary in respect of all government policies directly or indirectly affecting competition in general and acquisitions of control in particular, including policies towards foreign trade, foreign investment, industrialisation and structural adjustment, deregulation, privatisation, consumer protection and financial market and firm structures and governance. Competition policy should both constitute a key element in the implementation of such policies and be implemented separately through competition law controls upon RBPs in a consistent and coherent manner. This need for consistency is particularly important in respect of: trade policy, where the benefits of international trade liberalization may be reduced by anti-competitive conduct of firms, or where non-tariff barriers can lead to anti-competitive consequences in both importing and exporting countries; industrialisation and structural adjustment policies, which can promote either large firms or SMEs, or which can exempt certain sectors from the application of competition law; and deregulation and privatization policies, where it would be necessary to ensure that firms do not take advantage of the vacuum left by Governments' disengagement to undertake anti-competitive action. There is also a need, in order to minimize distortion of business decisions, to ensure consistency and a degree of neutrality in the application of competition law towards different types of RBPs, existing monopolies, greenfield investment, mergers, different types of joint ventures, and interlocking shareholdings and directorates, taking into account differences in their effects.

(vii) In recent years, a number of developed countries have adopted or reformed merger control laws or enforcement policies. Important differences exist in these laws or policies, but the similarities among them are far more important. There is now relatively greater reliance upon economic analysis of the likely effects of individual transactions and greater account taken of the internationalisation of markets. Questions of efficiency and of competitiveness are given weight in varying degrees and manners in different countries, but competition is usually the decisive criterion in the bulk of cases. However, there have occasionally been tensions over perceived conflicts between considerations of competition and of competitiveness, and these could well become sharper in future.

(viii) The overseas effects of domestic acquisitions of control are generally only dealt with to the extent that there is "spillover" onto the domestic market. The internationalization of production is likely to lead to such "spillover" happening increasingly often. Where overseas acquisitions of control affect domestic markets or (under United States law and enforcement policy) export trade, different doctrines are relied upon by individual developed countries to claim jurisdiction over such acquisitions of control. Such claims of jurisdiction, or their exercise, are often tempered by certain legal or enforcement principles such as comity. Despite the differences in the jurisdictional doctrines and tempering principles applied by different countries, similar results have often occurred in practice. This fact, as well as the growing adoption and use of bilateral, regional and plurilateral cooperation mechanisms, has minimized jurisdictional conflicts in recent years. Yet a potential exists for sharper conflicts in future because of continuing differences in the ambit and the exercise of jurisdictional claims, as well as because of economic globalization and more active competition law enforcement. More and more mergers are requiring approval by several competition authorities, sometimes leading to procedural problems and divergent substantive results as the competition analyses and interests of individual Governments will naturally differ.

(ix) A number of developing countries (as well as countries of Central and Eastern Europe) have adopted and are applying competition laws, including merger controls. The rapidity with which such laws are being adopted or reformed testifies to the increasing importance attached to competition policy. But problems are being experienced by developing countries in connection, *inter alia*, with: the lack of clear policy guidelines as to how to deal with the convergence and the potential tensions between competition and efficiency; lack of public awareness of what competition entails; lack of necessary data and trained staff; and lack of adequate fact-finding and enforcement machinery (including with respect to arrangements entered into overseas). Clearly, great efforts are necessary by developing countries aimed at: adopting or modernizing competition laws in tune with both the specific conditions relating to competition prevailing in their markets and with the current world environment, and dealing adequately with efficiency issues; creating or improving the necessary machinery to smoothly implement such laws; and undertaking the necessary pedagogical endeavours to raise public awareness of competition issues. Attention by competition authorities to lasting changes in market structure that could result from acquisitions of control is particularly important during the current transition in developing countries towards more market orientation, since market structure changes may help to determine the success of liberalization. Co-operation from other countries would assist developing countries in their efforts.

(x) Such efforts would also enable developing countries to better participate in any search for strengthened multilateral co-operation in this area. Such a search may be necessary because, in a world where markets have become increasingly interdependent, where enterprise transactions increasingly cross national borders, and where more competition laws are being adopted and effectively enforced, concurrent exercises of jurisdiction are bound to occur more and more often, sometimes leading to procedural problems and possible conflicts among different competition systems and decreasing enterprise security. Attempts by developing countries to gather information or to enforce their competition laws will increasingly have an impact on TNCs, for instance. Although the application of tempering principles such as comity in the enforcement of national law may reduce conflicts, these cannot provide a fully satisfactory solution, given their often discretionary nature, the lack of clarity as to their scope, and international divergences in their application. It is true that, to deal with such difficulties, there are a number of agreements among developed and Central and Eastern European countries in the area of competition. However, only the notification and consultation parts of these agreements have been used so far; nor do they deal with the question of cases brought by private parties. In any event, developing countries are not so far party to such agreements.

(xi) Apart from establishing mechanisms to resolve issues relating to concurrent jurisdiction, strengthened multilateral cooperation may be appropriate to obtain evidence, to build a consensus over individual cases, to address dangers of international oligopolisation in some industries, to avoid risks that enforcement efforts *vis-à-vis* national enterprises will be deterred by concerns over reducing their competitiveness as compared to enterprises based in countries where enforcement is less stringent and to coordinate unilateral or bilateral linkages that are being made between competition and trade. Suggestions are in fact being made in different quarters that normative links between competition and international trade should be strengthened to take into account the increasingly global context for the implementation of competition policy. In this connection, it may be recalled that national competition laws take no account of the effects of acquisitions of

control (including export joint ventures or cartels) upon overseas markets, and confidentiality is maintained where export cartels are registered. Continuing global specialization in production casts doubts about the tenability, in future, of sharp distinctions between effects upon domestic and foreign markets. Moreover, cartels can breed counter-cartels.

(xii) It may therefore be prudent for competition authorities to undertake informal exploratory discussions on the appropriateness of, and modalities for, progressively strengthening multilateral co-operation in the area of competition, to avoid having to react to problems in an *ad hoc*, hasty and uncoordinated manner. The consultation machinery provided for by the Set of Principles and Rules for the Control of Restrictive Business Practices would be well suited for such discussions.

(xiii) In the light of the above, possible action by States could include:

(a) The full implementation of all provisions of the Set of Principles and Rules, in order to ensure its effective application;

(b) The adoption, improvement and effective enforcement of appropriate competition legislation and procedures;

(c) Technical cooperation to assist such endeavours;

(d) Consultations in the context of the Intergovernmental Group of Experts to discuss the appropriateness, and to identify concrete ways and means, of improving transparency, information sharing, consultations and cooperation among Governments in respect of arrangements affecting competition, particularly in the markets of developing countries.

INTRODUCTION

1. The present study has been prepared in accordance with the agreed decisions and conclusions adopted by the Intergovernmental Group of Experts on Restrictive Business Practices at its sixth session,[1] and follows through from previous progress reports on this subject prepared by the UNCTAD secretariat.[2] It constitutes a revised version of the study initially prepared[3] and presented to the Intergovernmental Group of Experts on Restrictive Business Practices at its tenth session from 23 to 27 October 1991. At that session, the Group of Experts welcomed the useful work done by the UNCTAD secretariat on the said study and requested the secretariat to finalize a further draft of the study, taking into account the comments made at the session and written comments to be submitted by member States by the end of January 1992.[4] As requested, the present study takes fully into account the comments made at that meeting, as well as written comments made thereafter.[5] In addition, the secretariat has taken the opportunity to update the report in the light of the most recent data and developments.

2. As provided for in the mandate, this study deals with the effects on the domestic and export markets of developing countries of concentration of market power occurring through horizontal, vertical or conglomerate acquisitions of control. The types of acquisitions of control that are covered include mergers and take-overs (through transfers of shares or of assets, including through debt-equity swaps[6] and management buy-outs[7]), interlocking directorates or shareholdings (interlocks), joint ventures,[8] and privatization.[9] Thus, an acquisition of control need not necessarily involve a change in the legal ownership of an enterprise, but concerns rather a change relating to its *de facto* control (although joint ventures would in most cases involve the creation of a new entity or other collaboration by two or more enterprises). For the purposes of this study, "control" is interpreted in a broad sense to include the ability to materially influence the policies of an enterprise. In practice, of course, it may often be difficult to draw the line between "control"

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1 The Secretary-General of UNCTAD is thereby requested to prepare a "*study on the subject of the concentration of market power through mergers, take-overs, joint ventures and other acquisitions of control, whether of a horizontal, vertical or conglomerate nature, and its effects on international markets, in particular the markets of developing countries*". See "Report of the Intergovernmental Group of Experts on Restrictive Business Practices on its sixth session" (TD/B/1156-TD/B/RBP/43).

2 See the two papers entitled "Activities relating to specific provisions of the Set of Principles and Rules" (TD/B/RBP/48 and TD/B/RBP/60).

3 See "Concentation of market power through mergers, take-overs, joint ventures and other acquisitions of control, and its effects on international markets, in particular the markets of developing countries" (TD/B/RBP/80).

4 See the Agreed Conclusions adopted by the Intergovernmental Group of Experts at its tenth session, contained in the "Report of the Intergovernmental Group of Experts on Restrictive Business Practices on its tenth session" (TD/B/1310-TD/B/RBP/85).

5 Written comments were received from the Governments of Finland, Germany, the United Kingdom and the United States, and from the Commission of the European Communities.

6 The conversion of a debt instrument of a debtor country into an equity investment within that country. Typically, once an investment proposal has been approved by the competent authorites, the investor purchases the foreign currency debt at less than face value, converts it to local currency and proceeds to make the approved investment.

7 A transfer of company ownership of an enterprise where the existing employees are a significant element in the new set of owners. For the purposes of this paper, no distinction is made between buy-outs by a management team or by all the employees ("employee buy-outs").

8 For the purposes of this study, a broad definition of joint ventures has been adopted to include any arrangement "in which the operations of two or more firms are partially, but not fully, functionally integrated". See *Competition Policy and Joint Ventures*, OECD, Paris, 1986. The existence of equity stakes would thus not be necessary, so that contractual ventures and "strategic alliances" would be covered, although *ad hoc* agreements would be excluded. The acquisition of shares in an existing firm by at least two other firms would also be covered; this could also be considered to be a merger.

9 In this study, the emphasis is on privatizations occurring through partial or complete transfer of ownership from the public to the private sector (i.e. divestiture), rather than other arrangements not involving transfer of ownership or control.

(including material influence) over an enterprise and a degree of influence over its conduct which does not amount to material influence. The main emphasis of the study will be upon mergers and take-overs (the two terms will be used interchangeably) and, to a lesser extent, upon joint ventures. The parties to acquisitions of control having effects upon the markets of developing countries can be all locally established (whether foreign-owned or not), involve one locally established and one foreign party (e.g. the take-over of a local enterprise by a transnational corporation (TNC) or the take-over by a local enterprise of a foreign company), or be all foreign-based (e.g. overseas mergers of TNCs involved in trading or competing with developing country enterprises).

3. The study is divided into six chapters. Chapter I assesses what has happened (i.e. recent trends relating to different types of acquisitions of control), why it has happened, and the structural context in which it has occurred. In the light of these, the chapter then attempts to predict future trends. Chapter II describes some competitive conditions in the domestic and export markets and trade channels of developing countries which are relevant to an analysis of the effects thereon of acquisitions of control. Chapter III describes the beneficial and adverse effects upon the markets of developing countries, in terms of both concentration and market power, of acquisitions of control among local firms, in the light of the competitive conditions in developing country markets. Chapter IV looks at the effects upon the markets of developing countries of acquisitions of control involving foreign-controlled firms, including mergers or joint ventures between locally controlled firms and transnational corporation (TNC) subsidiaries or foreign-based firms newly entering the market, and overseas mergers or joint ventures among foreign firms. While there are important differences among these different types of acquisitions of control involving foreign-controlled firms, they are dealt with in the same chapter because the fact-finding and enforcement issues they raise are often similar.

4. Chapter V looks at the policy framework affecting acquisitions of control, including both the general framework of different types of economic policies directly or indirectly affecting competition policy and competition rules relating to different types of restrictive business practices (RBPs) which would have a bearing on competition rules governing mergers. Chapter VI examines the competition law treatment of mergers (with some references to joint ventures) in developed and developing countries, and then looks at existing mechanisms and possible future efforts for strengthening international cooperation in this area.

Chapter I

DEVELOPMENTS, MOTIVATIONS AND STRUCTURES RELATING TO ACQUISITIONS OF CONTROL

A. Developments during the 1980s

1. Mergers

5. The 1980s, particularly in their latter half, saw a massive increase in acquisitions of control. Particularly striking has been the merger activity in developed countries. Transactions involving United States companies are estimated to have totaled over $1.3 trillion during the decade.[10] Within the EEC, merger activity in the United Kingdom increased threefold between 1985 and 1988 to reach 57 billion ECUs, and in France sevenfold during the same period to reach 26.5 billion ECUs.[11] Merger activity in Japan, while relatively limited, has steadily increased, although contested bids are very rare. As compared with previous merger waves, distinctive features of mergers in the 1980s were their often very large value and cross-border character, and their predominantly horizontal nature (conglomerates have in fact been busily divesting during this period). The often contested nature of take-over bids, and the use of restructuring vehicles such as leveraged buy-outs, management buy-outs and junk bonds, particularly in the United States, have also been striking features of the merger wave. Merger activity has been prevalent in nearly every sector, some of the most affected including the food and food retailing, white goods, packaging, chemical/pharmaceutical, petroleum, paper, automobile and parts, telecommunications, airline, electromechanical, financial services, hotel, publishing and advertising industries.

6. However, the value of mergers in the United States is reported to have fallen from $US 264 to $117 billion from 1988 to 1991,[12] with a particularly sharp decline in leveraged buy-outs and (to a lesser extent) in contested bids in general. A less sharp decline has occurred in the United Kingdom. However, merger activity has declined far less in terms of numbers. Moreover, it has so far continued unabated among large firms in the European Community as a whole, where the number of mergers and acquisitions of majority stakes between 1988/89 and 1989/90 (June to May) increased by 25 per cent to 833;[13] the number of joint ventures increased by 20 per cent.

7. It is difficult to fully assess the extent of merger activity involving firms based in developing countries, given the lack of available data. However, it is reported that their participation in mergers has so far been relatively small (particularly in value terms), but that the growth rate of such activity has been significant in the case of enterprises from Latin America[14] and from the Far

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10 See S. Waite, "All the World's a Stage for M & A in the 1990s", *Mergers and Acquisitions*, September/October 1990, p.82.

11 See Booz Allen Acquisition Services' "Study on Obstacles to Takeover Bids in the European Community", p.13, prepared for the European Commission.

12 See "Steady stream of smaller deals", *Financial Times*, 11 June 1992.

13 See Commission of the European Communities, "Twentieth Report on Competition Policy", Brussels, 1991.

14 See Business International Corporation, *Profits under pressure in Latin America*, New York, 1985.

Eastern region.[15] Some domestic merger activity has occurred in Hong Kong, Malaysia, the Philippines and Singapore, including a few take-overs of local companies by companies from developed market-economy countries. There are also data indicating that there has been significant merger activity in these countries amongst TNC subsidiaires in the advertising and accounting sectors (following overseas mergers of parent companies[16]), and this may well have also been the case in other sectors. In the Republic of Korea, it is reported that there were 2,003 mergers in the decade 1981-1990, only 1,045 of which were among unaffiliated firms.[17] In the Philippines, mergers have taken place among both locally owned and foreign-owned companies in such sectors as electronics, textiles, mining and banking.[18] A few mergers have also occurred in India, in sectors such as the food-processing industry.

8. In recent years, firms based in the Far East have also become more active as buyers in the merger markets of developed countries (mainly the United States), although, of course, their involvement is tiny in relative terms. In 1989, for example, 16 take-overs in the United States were made by firms based in Hong Kong, four by firms based in Taiwan Province of China, four by Singaporean firms, and one by a Thai firm. Between 1986 and March 1992, a total of 35 overseas take-overs by companies for the Republic of Korea is reported to have taken place.[19] In general, firms from the Far East have tended to concentrate take-overs in such sectors as informatics, biotechnology, petroleum, hotels, food and distribution, but take-overs have also been made in other sectors. Government-owned enterprises have also participated in such take-over activity. The largest take-over by firms from the Far East to date appears to have been the $268 million acquisition of a United States company which is a market leader in computer terminals, with an extensive distribution network, by a consortium of companies from Taiwan Province of China, with the participation of a government development fund.[20]

9. Take-overs abroad by Latin American enterprises have been fewer, but are increasing rapidly. Merger activity within Latin America has been far more significant. During the economic crisis that hit most Latin American countries in the 1980s, there appears to have been substantial divestiture by TNCs of their Latin American subsidiaries. These sales were either to local investors (sometimes through management buy-outs) or to other TNCs, although foreign investment régimes in some countries have been perceived as discouraging the latter. In cases of sales to local groups, divesting TNCs have often tended to maintain contacts with their former subsidiaries through minority shareholdings, licensing or technical assistance arrangements, or joint ventures. On the other hand, other TNCs have taken advantage of the "buyers' market" created by the economic situation to take over subsidiaries of other TNCs, the interests of joint venture partners or independent local firms. Take-overs have often been linked with debt-equity swaps, particularly in Brazil and Chile, since these countries have allowed swaps for private sector as well as public sector debt. Between 1986 and 1990, debt-equity swaps yielded debt reductions in Brazil and Chile in the order of $9.5 and $6.5 billion respectively.[21] In Brazil, only foreign investors were allowed to take advantage of swaps, while in most countries local residents have also been eligible. However, restrictions have been placed on debt-equity swaps in several countries, which now tend to use them only for privatizations.

10. In Africa, there have been cases of take-overs by TNCs of subsidiaries of other TNCs operating in Africa in such sectors as food processing, fertilizers and textiles (in Zimbabwe) or pharmaceuticals (in Senegal).[22] But there have also been instances of foreign firms acquiring shares or assets of local private companies, as in the transport sector in Zambia, or in the textile sector in Togo. Debt equity swaps involving private companies have been few, given the fact that most debt

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15 See "How Pacific Rim Buyers Are Hitting the World M & I. Scene", *Mergers and Acquisitions*, Vol.25, No.1, July/August 1990, p.26.

16 See Sieh Lee Mei Ling, "Professional Business Services in ASEAN and the Uruguay Round Trade Negotiations", *Services in Asia and the Pacific: Selected Papers*, Vol.I (UNCTAD/ITP/51).

17 Information provided by KPMG San Tong & Co., Seoul.

18 See "Policies on competition and restrictive business practices in the Philippines", (UNCTAD/ITP/63), consultant report prepared for the UNCTAD secretariat by G. T. Santos.

19 Information provided by KPMG San Tong & Co..

20 See "How Pacific Rim Buyers Are Hitting the World M & I.. Scene".

21 See UNCTC report, "Transnational banks and debt-equity conversions" (E/C.10/1991/5).

22 See Page S. and Riddell, R., "FDI in Africa: opportunities and impediments", *The CTC Reporter*, No.27 (Spring 1989).

is owed to Governments, but some swaps have occurred in countries such as Zambia. There has been some merger activity in Kenya between both small local firms and larger subsidiaries of TNCs whose parents have merged (although, in the latter case, the recently established competition authorities have begun to block mergers).[23]

11. In some developing countries, gradual transfers of ownership of enterprises from foreigners to nationals, or between ethnic groups, have occurred as a result of "fade-out" or "indigenization" regulations. In Nigeria, for example, it is estimated that out of some 1,200 enterprises affected by the Nigerian Enterprises Promotion Decree 1977, 930 had been transferred to Nigerians by 1985.[24] In Malaysia, where a Foreign Investment Committee regulates take-overs by both foreign and local companies, taking into account such factors as the extent of Malaysian, particularly indigenous Malay (Bumiputra), participation and a number of other socio-economic factors, between 1971 and 1990, ownership of corporate wealth by foreigners was reduced from 63.3 to 25.1 per cent, while ownership by Bumiputras was increased from 2.4 to 20.3 per cent.[25] However, the implementation of such legislation has since been liberalized in both countries, as has similar legislation in some other developing countries (at least in respect of transfers from foreigners).

2. Joint ventures

12. The 1980s have seen an increase in the use of joint ventures by enterprises of many countries from all regions. In developed countries, there has been a particularly sharp increase in cross-border joint ventures, as well as in new types of "strategic alliances", especially with regard to research and development, and the introduction of new production methods. Some of the sectors where joint ventures have been prevalent include the informatics, electronics, robotics, telecommunications, aerospace, automobile and parts, and chemical/pharmaceutical sectors. In general, joint ventures have been formed more readily in high-technology areas, in contrast with mergers, which cut across all sectors. The nature of the ventures formed, and the closeness of collaboration, has varied greatly. In developed countries, it has also become increasingly common for companies to take minority stakes and/or cross shareholdings in each other in the context of technological or industrial cooperation or licensing arrangements. This practice is very prevalent among Japanese companies where there are numerous coalitions of interlinked companies (the most closely linked of which are called the "keiretsu"). A few United States companies are starting to follow this example by taking stakes in suppliers, customers and distributors.

13. The countries of Eastern Europe, China and some technologically advanced developing countries have seen sharp increases in numbers of joint ventures formed between local and foreign enterprises, although these have usually been of the traditional kind, rather than the new kinds of "strategic alliances". A large proportion of joint ventures in some developing countries has been in such industries as electronics and electricity, fabricated metal, chemicals, automobiles and parts, industrial supplies, food, and machinery and tools. In many developing countries which are less technologically advanced, however, joint ventures have been confined to a few industries such as the pharmaceutical, agro-industrial or mining sectors.

3. Privatization

14. Privatization has taken place on a massive scale in a large number of countries over the last decade. The pioneer among developed countries was the United Kingdom where, by April 1989, proceeds from privatization totalled over £24 billion pounds sterling.[26] This example was rapidly

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23 Statement made by Kenyan delegation during the Second United Nations Conference to Review all Aspects of the Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices.

24 See F. Beveridge, "Taking Control of Foreign Investment: A Case Study of Indigenization in Nigeria", *International and Comparative Law Quarterly*, Vol.40, April 1991, p.302, at p.317.

25 See "Mahathir offers new policy initiatives", *Financial Times*, 18 June 1991.

26 See "Privatization in the United Kingdom", Background Briefing, by Her Majesty's Treasury.

followed by other developed countries. Extensive privatization programmes are also being implemented in the countries of Central and Eastern Europe. Among developing countries, a few had already undertaken limited privatization during the 1970s, but major programmes by many countries only began to be implemented during the 1980s, resulting in the transfer to the private sector of a large number of enterprises in all sectors. A sample of 10 countries studied in a recent OECD report[27] had, for example, carried out more than 200 operations. Chile has, since 1985, privatized 38 enterprises for approximately $1 billion. Privatization has assumed a key policy role and has been incorporated in economic adjustment programmes of many countries, particularly in Latin America and sub-Saharan Africa, often under the advice of international financial institutions. However, the difficult privatization process has been relatively slow, and many of the enterprises privatized have been among the smaller ones. Complete disposals of enterprises have been relatively rare and many developing countries have realized little capital from privatization, although they may thereby have succeeded in reducing budgetary expenditure.

15. The techniques of divestiture through privatization have included public share offerings, transfers of equity or assets (including through debt swaps), management buy-outs, and unsubscribed increases of capital. Innovative new methods are now being tried in Central and Eastern Europe. Privatization techniques without divestiture have included leasing, concessions management contracts, subcontracting, licensing, and franchising. Public offerings have been used much more in developed than in developing countries, where the favourite method of privatization has been through complete or partial sales of shares or assets to private purchasers. The largest number of sales has been made to local firms, but the average value of such sales has often been very low, and the average value of sales to foreign investors far higher, in most developing countries. Larger-value sales, particularly those in the financial, transport and communications sectors, have in fact tended to depend upon foreign involvement or public share issues. The acquisition of foreign controlling stakes in key national industries through privatization has been a recurrent concern in countries from all regions, and mechanisms such as limitations upon the percentage of shares that can be acquired by foreign investors, or the placement of controlling stakes with trusted national firms (as in the French privatizations) have sometimes been used to maintain national control, as well as for other reasons. Some "strategic" sectors have usually been excluded from privatization in every country.

B. Motivations

1. Acquisitions of control of private firms

16. The impetus for a merger usually comes from the managers of the acquiring firm. Their motivations may be characterized as being speculative, personal or based on long-term economic considerations. With regard to the latter, a number of possible reasons may explain why the acquiring firm chooses to merge and acquire the assets of another firm in a "packaged" form, rather than to expand through internal growth, such as: the possibility of acquiring extra capacity faster, more easily, or for less cost, without leading to over-capacity; tax advantages; obtaining access to technology and production experience, and the facilitation of R and D; sales maximization; and the acquisition of market power. Some of the above-mentioned motivations also explain the formation of joint ventures. Their limited and flexible nature, their lesser cost, risk-sharing possibilities and the multiplicity of the links possible may make them preferable for some enterprises. Data gathered by the European Commission[28] lists the following as stated motives for large mergers and joint ventures within the EEC: the reinforcement of market position (by far the most important motive for mergers), expansion, complementarity, diversification, restructuring, R and

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27 See, O. Bonin and Ch.-A. Michalet, *Rebalancing the Public and Private Sectors: Developing Country Experience*, OECD Development Centre, Paris, 1991.

28 See "Twentieth Report on Competition Policy".

D, cooperation, other and unspecified motives.

17. The large numbers of mergers and joint ventures in developed countries that have occurred during the 1980s were also certainly influenced by the prevailing economic and financial environment, and indeed form part (in respect of cross-border mergers) of the larger phenomenon of the growth in foreign direct investment. The economic growth experienced in developed countries, the globalization of markets and of production, the greater intensity of competition, and the greater importance of "speed-to-market", services, product differentiation and quality have all played a role. The speed of technological change has necessitated greater financial capacity, higher production volumes and sales, and speedy and extensive penetration of world markets so as to amortize costs and diversify risks. On the other hand, in declining or low-growth industries, greater competition has necessitated the acquisition of existing assets to get them off the market. The presence of many willing sellers on the market, strong company profitability, the easy availability of finance, anomalous stock market valuations, favourable tax environments and liberalized regulatory controls on mergers in a few countries, and foreign investment liberalization all provided appropriate opportunities. The activity of individual firms has stimulated their competitors to follow suit to avoid falling behind, while mergers have often been followed by subsequent divestment of unwanted units.

18. Many mergers or joint ventures within the European Community have been undertaken by a desire to be optimally placed to benefit from the Community's integration process, while foreign acquirers appear additionally to have been motivated by fears of protectionism. The influence of regional integration processes has also been evident in merger activity involving Canadian companies, and has influenced acquisitions by TNC subsidiaries in some Latin American countries,[29] although regional integration schemes by developing countries have not led to any large inflow of new foreign investment. Regional integration trends are now stimulating take-overs of Argentinian enterprises by Brazilian and Chilean firms.

19. Take-overs by foreign firms of local companies in the Far East have been mainly because they have assets otherwise difficult to obtain (e.g. holding companies); in other cases, relatively high stock market valuations or expanding product markets may have made building plant more attractive, or market entry conditions have made joint ventures preferable (by contrast, as noted above, in Latin America, depressed economic and financial conditions, low valuations and debt-swap programmes had stimulated both buyer and seller interest in mergers). Indeed, in many developing countries, foreign investors, especially smaller firms, have preferred joint ventures because of the risks associated with operating in an unfamiliar environment, the limited importance of individual markets, the opportunity to take advantage of a local firm's market entry and knowledge advantages and regulatory entry barriers. Local firms in developing countries hope to gain by participating in projects which would otherwise remain beyond their reach financially or technologically, and by having the assistance of their foreign partners to export. Developing country enterprises take over enterprises in developed countries, or acquire minority stakes, mainly in order to obtain access to markets, distribution networks, technology, and essential raw materials or feedstocks.

20. Mergers among local firms in Hong Kong, Malaysia and Singapore appear to have been motivated by the desire to diversify from declining industries, to rescue failing firms (where banks may play a role), or to acquire companies holding land, as well as by speculative motives. In the Philippines, however, the desire to improve competitiveness, to minimize competition, or to monopolize trade has played a role. In the Republic of Korea, it is reported that most mergers were driven by government policies or financial and tax benefits.[30] However, motivations that have been reported to the Fair Trade Commission have included diversification, improvement of financial structures, rationalization of production processes, upgrading of distribution systems and "disintegration".[31] In recent years, there has been a growing trend towards divestment by conglomerates in order to specialize; one large group, for example, has divested US$ 3 billion worth of business since 1989.[32]

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29 See *Profits under pressure in Latin America*.

30 Information provided by KPMG San Tong & Co., Seoul.

31 See "Corporate policies in Korea".

32 See "Samsung: Korea's Hope for High Tech", *Business Weekly*, 27 January 1992.

2. Privatization

21. The objectives of privatization in different countries have coincided to a large extent, although the breadth and the relative emphasis accorded to different objectives have varied from time to time and from country to country. The related objectives of raising capital and reducing recurrent budgetary expenditure have been crucial, particularly for developing countries. Another related set of objectives has been the withdrawal of the state from commercial activity, and the development of the private sector, private investment and entrepreneurship, capital markets, and wider share ownership. It has also been hoped that this would send favourable signals to foreign investors. The attainment of efficiency at the level of individual enterprises has been a key objective, given the inefficiencies of many state enterprises, while it has also been hoped that the transfer of assets into private, competitive markets would promote efficient pricing of goods and services through the elimination of monopoly profits and would engender greater responsiveness of the economy to changing conditions. The above-mentioned objectives, however, have sometimes been in conflict. Such conflicts have arisen, for example, from the fact that it would usually be easier to obtain financial gains quickly from the sale of the most efficient and profitable state enterprises, or that a reduction in the monopoly powers of a state enterprise might deter potential purchases, or reduce the price that could be obtained from its privatization, the further investment the acquirer would undertake or the viability of the enterprise.

C. Influence of industry, financial market and firm structures

22. The structural characteristics of a country's industry, capital markets and firm organization necessarily determine the extent to which acquisitions of control can take place and the type of acquisition favoured. Traditionally, companies based in the United Kingdom and United States have been the most "open" to take-over; 99 per cent of the largest United States based firms are quoted on the stock market, for instance, as compared with 54 per cent of the largest European Community firms.[33] In some European countries, the existence of classes of shareholders without voting rights, relatively small fractions of active shareholders, the influence and shareholdings of banks or state-owned companies, family-controlled structures, or internal regulations of companies may tend to raise barriers against contested take-overs. Of course, some of these factors may sometimes make it easier to mount take-overs by reducing the number of shareholders to influence. The general trend in Europe appears to be towards a reduction in barriers to take-overs. However, in the United States, the powers of management to resist unsolicited bids have recently been strengthened in some states.

23. In developing countries, structural characteristics such as the relatively high proportion of industry in state ownership, the relatively small number of firms (out of which few are public limited companies accessible to outsiders), and the high concentration of ownership have all tended to limit the number of mergers taking place and favoured internal growth instead. Groupings of family controlled companies which control a relatively large share of industry are common in some developing countries. In general, the prevalence in developing countries of owner-management rather than professional management, cultural inhibitions that may exist about acquiring other firms (particularly through contested bids), the non-existence or small size of stockmarkets and difficulties in obtaining finance for take-overs would act as brakes to mergers. Of course, the extent to which such structural characteristics are prevalent varies from country to country. It should be noted that structures in developing countries have already changed somewhat, taking into account privatization, the larger number of firms operating in some more advanced developing countries, the greater size, sophistication and activity of stock exchanges, and growing capital accumulation in a few developing countries.

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[33] See Booz Allen Acquisition Services, *op.cit.*.

D. Possible future developments

24. During the current decade, developments relating to acquisitions of control would of course depend upon broader macro-economic changes which are difficult to predict. Yet many of the macro-economic and technological factors that have contributed to the rise in mergers and joint ventures throughout the 1980s continue to exist. Merger activity in developed countries has always been cyclical in nature, and the late 1980s may have seen the peak of one such cycle, at least in the United Kingdom and the United States. It appears likely that, for the next few years, less liberal finance will continue to result in a decline in transactions undertaken for speculative or financial reasons, and thus in the size of transactions, while the failures of many mergers and joint ventures should induce caution. However, the financial difficulties of companies in a period of slower growth, the effects of deregulation and privatization, the need for merged companies to divest some units in order to reduce debt, to rationalize capacity, and to concentrate on core businesses and the opposite desire to expand geographical reach and market share should result in a steady stream of deals. Shortages of venture capital in high-technology sectors could stimulate take-overs, particularly of start-up companies. Links among companies which have started off as joint ventures may be developed into mergers, although lack of finance for mergers is also encouraging the formation of more joint ventures and the acquisition of minority stakes instead. Foreign take-overs of firms in Eastern Europe, in connection with privatization, are likely to continue for some time.

25. Taking into account the ongoing structural changes noted above, a gradual increase in the participation in merger activity of developing country enterprises appears likely. A particular mention may be made in this connection of the strong trend towards liberalization. The removal of entry barriers implicit in deregulation, including foreign investment and trade liberalization, may lead to more mergers and joint ventures as established firms strive to preserve their market positions in a more competitive environment. Large-scale privatization in developing countries has, and is going to, allow more firms to merge. Given the size of assets in the public sector, financial problems, the need for massive investments in infrastructure, and fundamental changes in concepts about the appropriate role of the state, privatization programmes look set to continue for a long time to come. Liberalization of outwards investment and foreign borrowing by developing country firms should also increase overses takeovers by them.

26. Other factors that could encourage some developing country enterprises to seek mergers include: a desire to diversify from the home market because of growing foreign competition; a desire to diversify from the United States market by acquiring European companies; growing "South-South" investment, which should occur in some cases through mergers; succession difficulties of family-owned companies (these are also relevant in continental Europe); growing "openness" of stock exchanges, and the growing possibilities for large developing country firms to raise capital in local and international capital markets, thus funding acquisitions. (Conversely, greater ease in raising capital may decrease the need to merge of many Latin American firms.) Steady increases in joint ventures in many developing countries should also continue, as the growth in the numbers and capabilities of local firms creates more valid interlocutors for foreign partners, although concerns about protecting technology and creating new competitors may act as a brake. However, the above observations are subject to the caveat that it remains to be seen what the impact of economic and technological changes will be on foreign direct investment volumes, directions and strategies. If present trends relating to volumes and directions of foreign direct investment continue, many developing countries will face stagnation in incoming flows of foreign investment, necessarily resulting in low rates of mergers and joint ventures involving foreign partners. It is rather more certain that acquisitions of control involving only domestic firms will have a high growth rate in developing countries.

Chapter II

COMPETITIVE CONDITIONS IN MARKETS AND TRADING CHANNELS OF DEVELOPING COUNTRIES

A. Domestic markets and import channels

27. In assessing the effects of acquisitions of control upon the markets and channels of developing countries, the specific competitive conditions in these markets should be considered, taking due account of the sometimes very substantial differences in the conditions prevailing in different developing countries. In general, domestic markets of developing countries are characterized by relatively low demand, because of either limited purchasing power, size and/or sophistication. This would be true both of ultimate and of intermediate consumers; the small size of industrial sectors would reduce demand for capital goods and producer services, for instance. Given relatively low demand, and given that the manufacture of most products requires minimum economic scales (MES) below which it would be uneconomic to produce, the number of manufacturing plants (and hence, indirectly, the number of firms) in any particular sector that domestic markets in most developing countries would by themselves be able to sustain would be relatively low, resulting in a relatively high degree of concentration in different product markets.

28. The fact that the market concentration/economies of scale relationship is a relatively more significant feature of domestic markets of developing countries was confirmed by a statistical comparison of the correlation between industrial concentration and size elasticities of output per employee (as a proxy for scale economies) in selected developed and developing countries. A comparison in these countries of the same industries confirmed that, in many of these industries, there were inverse correlations between concentration and either or both the variables of level of industrial development and country size.[34] This state of affairs may be affected by technological change, which may sometimes make it economic to produce for small markets. But in any event, the installation of flexible production machinery has so far been much more extensive in developed than in developing countries.

29. Apart from low market demand, other market conditions often found in many developing countries which sometimes favour high concentration are: narrow and unbalanced economic bases and industrial structures; limited supplies and/or high prices of managerial, technological and marketing skills, of raw materials, machinery and spare parts, and of capital, all of which would be foreclosed by already established firms; inefficient distribution systems and transport and communications networks, which would raise transport costs and reduce the possibilities for competition to arise from sources which are further away (although, in the national market as a whole, this may decrease concentration by allowing more local firms to produce on a small scale); poor information flows often leaving customers unaware of available cheaper prices or alternative products or product sources and producers unaware of market opportunities; the lack of an entrepreneurial culture, or an insecure business environment which makes entrepreneurs seek rapid returns from trading rather than long-term investment; the non-existence or inadequate implementation of controls on anti-competitive practices; and regulations which restrict or discourage new market entrants (although, as discussed below, these may sometimes lead to reduced concentration and they are, in any event, being liberalized).

30. Thus, in India, for example, it is reported that the four-firm concentration ratio is between

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[34] See UNIDO publication prepared by H. Forstner and R. Ballance, *Competing in a global economy*, Unwin Hayman Ltd., London, 1990.

80 and 100 per cent in over half of the industries; this has been ascribed to restrictive industrial licensing regulations.[35] In the Republic of Korea, in 1988, the share in manufacturing value-added of the 10 largest *jaebol* (large conglomerate business groupings) was 12.5 per cent, while in 1990, the combined sales of the 4 largest *jaebol* amounted to more than half of the Republic of Korea's gross national product.[36]

31. While liberalization of foreign investment controls and subsequent competition from local production by foreign-controlled firms may help in some cases to reduce market concentration in developing countries, its impact may be uneven or limited in scope. In India, for example, TNCs' market shares are high in those branches of manufacturing characterized by a high degree of product differentiation , technology intensity or skill intensity and profitability.[37] This would suggest that TNC subsidiaries and local enterprises often concentrate upon different industry sectors or segments, with TNCs focusing upon segments where more prosperous customers accept higher prices. Ample confirmation exists of such a tendency in different service sectors within a number of developing countries; a dual market structure often emerges whereby an oligopoly of TNC affiliates service other TNCs and large local firms, offering expertise and world-wide networks and reputation, while local service firms compete intensely for smaller clients, offering lower price and cultural affinity.[38] In some cases, local firms have managed to emulate TNCs' skills and to compete with them, while TNC competition has sometimes led to reduced concentration and lowering of prices by local firms. But, in general, there is ample evidence showing positive correlations between the foreign-owned share of developing country industries (measured as foreign production in relation to total production) and indices of concentration.[39] It is not clear whether this is due to the results of TNC domination of an industry, or whether it is because TNCs are attracted to industries where entry barriers or economies of scale allow them to earn above-average returns. It may also be noted that foreign investors have on occasion pressed for trade protection as a condition for investing; this has happened in several instances, in Central and Eastern Europe, for example.[40]

32. Of course, even in developed countries, TNCs usually concentrate on certain market segments where they can best make use of the advantages they derive from their special skills and global reach. However, the lesser competitiveness of local firms in developing countries would increase possibilities for TNCs to dominate such market segments, thus replacing a less efficient local oligopoly by a foreign oligopoly. The evidence confirms that TNCs in developing countries generally have higher rates of labour and total factor productivity than domestic firms.[41] Even apart from such constraints, a number of economic factors have led to a stagnation of investment flows to many developing countries during the 1980s, as noted above. The establishment of an attractive environment would be essential for foreign investment to occur, but equally, the establishment of a competitive environment would be essential if the potential benefits of foreign investment in strengthening competition and spurring efficiency in developing countries are to be maximized.

33. Given the import liberalization that has occurred in many developing countries, competition between domestically produced and imported goods in developing countries could have a rather more extensive effect upon market concentration than would foreign investment. As the effect of import barriers may sometimes be to allow some producers to survive despite sub-optimal scales of production and high costs, foreign competition may sometimes strengthen industry concentration by reducing prices, thereby leading to market exit by some local firms and more intra-industry specialization and trade by TNC subsidiaries. Thus, in Chile, import liberalization between 1967 and 1979 led to a decrease in the mean price-cost margin from 48 to 32 per cent, an increase in the four-firm concentration ratio from 49 to 61.5, a decrease in the number of firms,

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35 See "India Survey", *The Economist*, 4 May 1991.

36 See "Time to cut giants down to size", *Financial Times*, 10 April 1991.

37 See, Kumar, N., *Multinational Enterprises in India, Industrial Distribution Characteristics and Performance*, Routledge, London and New York, 1990.

38 See UNCTC report, "Impact of transnational service corporations on developing countries" (E/C.10/1991/6). See also Sieh Lee Mei Ling, *op.cit.*.

39 See *World Investment Report, 1992*, "Transnational corporations as engines of growth" (ST/CTC/130), United Nations, New York, 1992.

40 See "Free trade and foreign investment in Central europe", *East West* (Fortnightly Bulletin), No.507, p.2, 15 July 1991.

41 *See World Investment Report*

and an increase in intra-industry trade.[42] Similarly, in Brazil, where recent tariff cuts have led to complaints about reduced competitiveness, a United States-owned manufacturer has had to reduce its prices and is now weighing the costs and benefits of producing each product locally rather than importing.[43] As the above examples would indicate, despite leading to higher concentration, the global effects of imports upon the competitive situation in developing countries may be often positive in terms of greater competition, reduced prices, and efficiency benefits from specialization.

34. However, foreign competition is far from being a perfect substitute for domestic competition. Imports may be relatively highly priced, aim only at certain sectors of the market, or (if they come from the same group as a locally established TNC subsidiary) avoid competing directly with goods produced by the subsidiary. Some products are inherently local or national in character, while competition from imports would also not usually be relevant in service sectors. The most serious obstacle to imports in most developing countries is lack of foreign exchange. In this respect, it is clear that developing countries cannot earn such foreign exchange unless they are given the opportunity to do so through exports, suggesting a direct link between developing country exports and competition in their domestic markets.

35. The effects of imports in strengthening competition are also often reduced, on the demand side, by foreign exchange fluctuations and lack of information on the available range of suppliers and, on the supply side, by such entry barriers as low market demand (reducing the numbers of foreign exporters, intermediaries and local distributors involved), transport difficulties and costs, tariffs, internal regulations, intellectual property rights, lack of market information, or distribution difficulties. When it is sought to import technology, its availability and the conditions governing access to it (such as limitations upon size or volume of production) would also be relevant. The use of other restrictive business practices may also, depending upon individual cases, affect the contribution of imported goods upon competition in developing countries.

36. Thus in Mexico, substantial tariff reductions have not brought domestic prices into line with international ones because, *inter alia*, of limited distribution channels, the quasi-monopoly of existing channels by "traditional" importers, and TNCs' discriminatory price policies.[44] The initial experiences of Argentina would indicate that competition from imports may be more effective in lowering manufacturers' input prices than retail prices.[45] Even in developed countries with a large import share, such as Norway, there is ample evidence that imports do not always result in more effective competition, partly because of differing costs, but mainly because foreign exporters may take advantage of high domestic prices to reap monopoly profits. The situation has been well summed up in the following words "... if competition is efficient in a market, the existence of international trade will strengthen and maintain the competition. If the competition situation is very weak, imports alone will not improve matters much".[46]

37. Moreover, premature exposure of developing country firms to "imported competition" may decimate infant industries and lead to concentration of market power in foreign exporters (particularly where "dumping" or government-subsidized pricing occurs), or in trading intermediaries, taking into account that a relatively small number of large firms undertake the bulk of exports from some countries (i.e. export concentration in these countries is significantly higher than industrial concentration) and that only some of these firms would be exporting to individual developing countries.[47] High concentration also exists in import channels of developing countries. In Côte d'Ivoire, for instance, 11 per cent of importing firms (i.e. 33 firms) accounted for almost 62 per cent of total importation in 1983.[48] These importing firms include both locally owned and

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42 See T. Condon and J. de Melo, "Industrial Organization Implications of QR Trade Regimes: Evidence and Welfare Costs", Working Paper No.487, World Bank, August 1990.

43 See "Business Latin America", *Business International Inc.*, 8 October, p.318.

44 See de Maico, F., "Trade, Technology and Competitive Opportunities", in *Competition and Economic Development*, OECD, Paris, 1991.

45 See "Painful embrace of a competitive transformation", *Financial Times*, 18 June 1991.

46 See Bakke, E., "Competition and International Trade", in *Competition and Economic Development*.

47 For data on the United States, see Forstner and Ballance, *op.cit.*, pp.154-159. See also Department of Commerce, "Report of the President on Export Promotion Functions and Potential Export Disincentives", 1980, pp.5-10. For data on the United Kingdom, see M. Utton and A. Morgan, "Concentration and foreign trade", Cambridge University Press, Cambridge, 1983.

48 See ITC report, "République de Côte d'Ivoire - Analyse du rôle et des performances des différents types d'entreprises dans le commerce extérieur", 1987.

foreign owned firms. A significant proportion of developing country imports is, in fact, channelled through the foreign trade establishments or affiliates of TNCs, or through transnational trading corporations (TTCs).[49] TNC affiliates often act on an exclusive basis for the distribution of all the parent's products. In certain markets, and particularly smaller ones, they may also hold exclusive importation and distribution rights for products of other TNCs. In several sectors, the major TNCs have established global networks of trading affiliates.

38. Among TTCs, the share of agency houses in Western European exports to developing countries, although declining in recent years, continues to be around 10 to 20 per cent, with a relatively larger share of exports to small and low-income developing countries. Another type of TTC, the general trading company (such as the Japanese *sogo shosha*) handles a significant percentage of world trade. The share of the *sogo shosha* (some of whom form part of the *keiretsu*) in the total trade of Asian and Pacific countries, for example, was estimated at about 17 per cent at the beginning of the 1980s, although this share may have gone down since then; their shares of import trade (and profit margins) were relatively greater than their export trade shares and margins. Still another type of TTC, the commodity trader, is particularly prominent in the international trade of agricultural commodities, particularly in smaller developing country markets. The mergers that have taken place in the 1980s, both among TNC marketing affiliates (consequent upon the merger of their parent companies) and among TTCs, would therefore have had a direct effect upon concentration in developing country import channels. However, competition from some developing country traders has grown.

39. Apart from mergers, other arrangements that are affecting concentration in developing country import channels are: export joint ventures, cartels, or associations. Such ventures exist in several developed countries in a range of sectors, and action has sometimes been taken against them by competition authorities in other developed countries. In general, however, it would appear that, at present, the numbers of such joint ventures, and the share of world trade affected by them, would be small. In the United States, for example, exports controlled by registered Webb-Pomerene associations accounted for less than 2 per cent of total exports in 1981.[50] In Germany, there were 42 export cartels still effective as of December 1988; one new cartel was authorized that year.[51] In the United States, 18 certificates of exemption from antitrust laws under the Export Trading Company Act 1982 were granted in 1988; it is difficult to assess how many export cartels have not applied for such exemptions, in reliance upon their immunity under general antitrust law.

40. Given the lack of transparency that often prevails, it is not clear to what extent developing countries are affected by such joint ventures. A 1978 report by the United States Fair Trading Commission mentioned that 16 Webb-Pomerene associations had government agencies or trading firms as customers in Eastern European or developing countries.[52] A court case in the United States involved a cartel for the sale of antibiotics formed by six pharmaceutical companies, which affected both the domestic and export markets, including India.[53] In another case involving India, its Monopolies and Restrictive Trade Practices Commission opened an enquiry in 1988 into a collusive tendering arrangement among some Japanese suppliers of steel rolls, which were alleged to have followed prices set by the Roll Exporters Association of Japan.[54] In a recent case, the European Commission imposed fines of over ECU 15 million (US$ 18 million) on 15 European shipping firms for operating cartels and market-sharing arrangements on routes between France and some West and Central African countries.[55] Other agreements involving traffic between European and Africa are under investigation.

41. Although the aggregate impact of such joint ventures may therefore at present be relatively

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49 See *World Investment Report* 1992.

50 *Competition Policy and Joint Ventures*, OECD, Paris, 1986.

51 See UNCTAD, "Annual report 1989 on legislative and other developments in developed and developing countries in the control of restrictive business practices" (TD/B/RBP/61).

52 "Webb-Pomerene Associations: Ten Years Later". Such an association is one formed under the Webb-Pomerene Act, which exempts from the application of antitrust law export trade associations formed for the sole purpose of engaging in export trade, provided they meet certain conditions.

53 *Pfizer Inc., v. Government of India*, 434, U.S.308 (1978).

54 See UNCTAD, "Annual Report 1989 ..." .

55 See "ECU 15 million in fines are imposed on shipping firms", Antitrust and Trade Regulation Report, Vol.62, p.422, 2 April 1992.

small, taking into account the growing profusion of sources of supply, they may well be having a significant impact in specific geographical or product markets, particularly where the joint venture includes producers from different countries, where the developing country concerned has few trading partners, or where the sector concerned has a pervasive impact upon the entire economy - as in the shipping case mentioned above. There are grounds for believing their impact may increase in future (see chapter IV of this study). Moreover, export cartels can trigger the formation of import cartels in other countries. They also exist in some countries as a corollary of voluntary export restraints (VERs) undertaken in response to pressure from trading partners. VERs necessarily involve actions by exporting firms to limit the volume and, in some instances, to raise prices of exports of a given product to one country. However, there is a risk of "spillover" onto the domestic market where exporting firms exchange information to facilitate the operation of the VER, or where the export cartel comprises a large share of domestic industry output. Thus, VERs can reduce competition in both the importing and exporting countries. On the other hand, it may be noted that export joint ventures established in developed countries may in some cases be having a beneficial effect upon concentration in developing countries by allowing SMEs to pool their exporting efforts, although it appears that they are little used by such firms and mostly include larger-than-average firms in concentrated industries.[56]

B. Export markets and channels

42. The competitiveness of developing country enterprises may be reduced by the imperfect conditions in their domestic markets, as noted above. In the process of exporting, developing country enterprises would also need to take into account clauses in licensing arrangements that may limit exports, or fix prices, as well as purchasing practices of firms, import cartels, customers' brand loyalty, and marketing, distribution and transport difficulties and costs, as well as tariff or non-tariff measures, procurement policies, regulatory licensing requirements, and product standards. The factors mentioned above may all heighten the normal disadvantages faced by latecomers *vis-à-vis* market incumbents, who have built up "learning economies" and "first mover advantages" from cumulative production experience and marketing intelligence.

43. Of course, it is not only developing country firms which face such entry barriers or other factors. Thus, the Structural Impediment Initiatives (SII) talks between the United States and Japan have addressed such issues as the alleged tendency of interlinked Japanese companies to purchase amongst themselves, cartel practices in some industries, procurement policies in civil engineering projects, and distribution difficulties, while the French Government has complained about the alleged tendency of two United States-based telecommunications companies to purchase mainly from their affiliates.[57] Moreover, despite these above-mentioned factors, manufactured exports from developing countries as a group have grown rapidly, although such success has been limited to a relatively small number of countries. High export market penetration achieved by firms from some Asian countries has often been concentrated within a few major markets and in relatively few product areas, particularly in the electronics industry, thus implying vulnerability to anti-dumping actions or VERs.

44. Other developing countries which have a high dependence upon the exportation of a few commodities may face tariffs rising in accordance with the degree of processing, or the activities of import cartels, which have occurred primarily in the raw materials sector.[58] Even apart from the activities of such cartels, however, a significant degree of market concentration exists in, for example, the coffee processing, tea blending and packing, and chocolate manufacturing industries.[59] In order to defend their market shares, the industry leaders in these areas use such strategies as

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[56] See *Competition Policy and Joint Ventures*.

[57] See "France attacks US telecom practice", *Financial Times*, 25/26 May 1991.

[58] See *Competition Policy and Joint Ventures*.

[59] See UNCTAD, "Prospects for the world cocoa market until the year 2005" (UNCTAD/COM/5); UNCTAD, "Studies in the processing, marketing and distribution of commodities: The processing and marketing of coffee" (TD/B/C.1/PSC/31/Rev.1), and UNCTAD, "The marketing and processing of tea" (TD/B/C.1/PSC/28/Rev.1).

product differentiation, price discrimination, heavy promotional activity, technology leakage controls and mergers. In the coffee-processing industry, for instance, the number of industry leaders operating within the EEC decreased from 18 to 4 between 1979 and 1988.[60] In general, however, the vertical integration that prevailed in past years, with TNCs exercising control over the whole chain, from production to processing, trade and distribution, has greatly diminished, particularly in respect of those agricultural commodities which are traded at low stages of processing.[61] The role of vertically integrated TNCs continues to be somewhat larger in respect of processed agricultural commodities (such as processed cocoa from Brazil and West Africa, sugar and tobacco from Zimbabwe, bananas from Latin America and the Philippines, or tea from India and Kenya).

45. Commodity trade is much more concentrated than commodity production. International trading companies and commodity traders are particularly prominent in the trade of some agricultural commodities, such as tea, coffee and bananas. Around half of world coffee trade is carried out through them, for example, while the large processing companies account for most of the remaining half. However, private and public sector companies from many developing countries have come to play an increasingly important role in export channels for commodities. In general, the intensity of TNC involvement in commodity exports from developing countries varies according to individual countries and commodities, but continues to be relatively high, particularly in some African countries. Their role is also important in distribution and service activities. The key role of TNCs in respect of exports of several commodities from developing countries would be positive insofar as TNCs would often be better able to maximize sales of the commodity in question. However, reductions in exports may result where TNCs are prepared to sacrifice some gains in sales volumes for the sake of profit maximization per unit.

46. In the area of manufactured goods, a substantial proportion of the products exported by developing countries are "dedicated" or "captive". Retailing firms in developed countries directly import an estimated 20 per cent of exports from the Asian region, for example,[62] thus providing strong competition to trading intermediaries. Subcontracting arrangements, including original equipment manufacturing (OEM), also account, depending upon individual countries, for a substantial share of manufactured exports. Intra-firm trade between TNC subsidiaries and their parents or other affiliates also accounts for a significant proportion of developing country exports, although usually less than developed countries' exports. In other export channels for manufactures, trading affiliates of TNCs and TTCs share a substantial proportion of trade. The participation of developing country firms is relatively small, in overall terms, but is increasing, and is high in a few countries. It may be noted that TNCs and TTCs have strongly contributed to the growth of developing country manufactured exports. The question whether their role has sometimes been negative is discussed in paragraph 72 and 73 below.

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60 See Booz Allen Acquisition Services, *op.cit.*, p.9.

61 See ITC publication, "Structural change in export marketing channels of developing countries", 1988; and "Transnational corporations in African trade: Major trends in primary commodities" (E/ECA/89/26).

62 See "Structural change in export marketing channels of developing countries".

Chapter III

EFFECTS UPON DEVELOPING COUNTRIES OF ACQUISITIONS OF CONTROL AMONG LOCAL FIRMS

A. Effects upon competition

47. In developing countries, it may often happen that firms participating in mergers are so small that the effects upon market concentration are negligible. However, mergers among smaller players in the market can lead to reduced market concentration, by enabling them to attain the critical mass necessary to win market share from a monopolist or oligopolist. Market concentration can also be reduced where a conglomerate merger enables an outsider firm to enter a concentrated market, where a vertical merger enables the firms involved to better compete against other vertically integrated firms, or where a management buy-out of part of a firm's assets results in the creation of an independent new entity (such buy-outs are in any case unlikely to lead to competition concerns).

48. On the other hand, market concentration may be strengthened where a horizontal merger eliminates an actual or potential competitor. A vertical merger can also strengthen concentration at either level of integration if it provides the possibility of exercising monopoly or monopsony power over existing or potential competitors, raising entry barriers to potential market entrants by obliging them to enter at both levels. Conglomerate mergers can give rise to industrial concentration where there would otherwise have been a *de novo* entry into a market or where the financial backing of a wealthy parent enables the acquired firm to acquire or maintain a dominant position of market power. They can also raise aggregate concentration in the economy as a whole, so that economic power in the country is held in a few hands. The competitive conditions and the concentration of ownership in developing countries would heighten these risks.

49. Joint ventures, although they would often result in the creation of a new entity, may have many of the positive or negative effects upon market concentration which mergers have. Negative effects may arise, for example, where a venture eliminates existing or potential competition among the participants in the area of activity covered by the venture, acts as a vehicle for a cartel, provides the participants with the opportunity to collude in areas other than the venture, or results in market foreclosure for third parties. Much will depend upon the extent to which an individual venture involves activity close to the market place and upon its openness to participation, as well as upon the nature of the restrictions ancillary to the venture. A venture which would have little effect upon market concentration by itself may have a wider effect as a link in a chain of other ventures engaged in by the participants, while a merger may also have more significant effects where the protagonists are participating in joint ventures. It is particularly difficult to generalize about the effects of joint ventures because of the large diversity of types of ventures which exist.

50. Another category of acquisition of control, privatization, also raises complex issues. Privatization may reduce the monopoly power of a state-owned enterprise, or remove the possibility that state control or financial backing may put the enterprise concerned in a more favourable competitive position than private firms. On the other hand, privatization may merely transform a State monopoly into a more efficient private monopoly, particularly: where effective competition is not created or allowed in the sector (e.g. by not splitting up the enterprise, where this is feasible, or by licensing regulations restricting new entry); where the enterprise concerned operates a natural monopoly such as a utility service; where the cost of new entry is prohibitively high; or where the privatized enterprise can take advantage of its established product name, the vertical integration of deregulated activities with monopoly activities, or financial strength arising

from such integration.

51. Higher market concentration would make it more likely that the firm concerned will abuse its market power successfully collude (explicitly or tacitly) with the diminished number of other firms in the market to restrict output and raise prices, or that other firms will eschew vigorous competition with market-dominant firms. Conglomerate mergers may increase "multimarket contact" among sellers competing in different markets, making more likely each firm's independent choice of the joint profit-maximizing solution. Of course, it does not necessarily follow that this will happen. Thus, a Brazilian car company (formed by a merger of the subsidiaries of two American and German car manufacturers) holding 60 per cent of the Brazilian car market was found, after investigation by the authorities, not to have committed an "abuse of economic power" when it sharply raised its prices (since the prices were no higher than those of competitors), and also not to have adopted practices prejudicial to the market in its relations with its suppliers and consumers.[63] In a similar case in Poland (although no merger was involved there), the Polish Supreme Court ruled that the sole Polish car manufacturer (FSO) did not need to revoke its three-fold price increase, as ordered by the Anti-Monopoly Office, because - although FSO held a dominant position on the Polish market for medium-size cars - the Office was unable to prove that FSO had undertaken any monopoly practice.[64]

52. But strong concentration would certainly heighten the risk of anti-competitive practices. Thus, concentrated product markets in manufacturing in the Republic of Korea, particularly where they are highly protected, have higher profitability than competitive markets, suggesting rent-seeking behaviour. It may also be noted that mean price cost margins are lower in sectors with high export shares, suggesting that competition in international markets makes domestic pricing also more competitive. However, there is little evidence of other anti-competitive behaviour. Out of 293 market-dominating firms designated by the Korean Fair Trade Commission in 1990, only 10 were found to have abused their positions through false allegations about other firms, tying arrangements and predatory pricing.[65] Nor has high concentration reduced the intensity of the rivalry among the *jaebol*, a factor which has certainly enhanced their competitiveness.

53. The likely effects of an acquisition of control should be evaluated in a dynamic context since a greater market share may not necessarily lead to a durable acquisition or increase of market power by the new entity or a significant decrease in competition. Effective competition can continue to exist in oligopolistic markets. Recent or ongoing changes in the market which may arise, for example, from new entry or technological change may lead to a diminution of market share, as may internal financial or efficiency problems. Customers or suppliers may have countervailing buying or selling power. Any market power attained may not exist for a long duration, since it may reduce demand, induce customers to search for alternative products or product sources, or stimulate new entry. The very threat of this happening may deter abuse of a dominant position of market power. Much would depend upon entry barriers to the market (which are high in developing countries), its structure and its rate of growth.

B. Effects upon competitive efficiencies

54. Moreover, mergers can lead to greater efficiencies in relation to investment, management and organization, production, sales or technological innovation (these are of course interrelated). Mergers would often be speedier and more convenient means of attaining such efficiencies, and of acquiring assets in a packaged form, than internal growth. Not only may such efficiencies occur within the merging firms, but spin-off effects can occur within the industrial sector, among suppliers or even within the whole economy. Of course, competitive markets in themselves usually provide the best means for encouraging economic efficiency by leading to the flexible allocation

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63 See "Autolatina beats anti-trust suit", *Financial Times*, July 1991.

64 See *East West* (Fortnightly Bulletin), No.506, p.11, 26 June 1991.

65 See "Corporate policies in Korea". Such firms are designated annually. For a firm to be considered to be in a "market-dominating position", it must have a monopolistic, duopolistic or oligopolistic position in a market with total domestic sales amounting to more than $45 million in the previous year.

of resources among competing uses in accordance with consumer preferences or technological possibilities, by putting pressure on firms to perform efficiently and to innovate, and by protecting consumers from exploitation. Conversely, efficiency gains are procompetitive where their attainment permits merging firms to better compete with other firms, particularly if any cost savings are passed on to the consumer; consumer welfare is enhanced by an efficient market structure guaranteeing more competition. In some circumstances, however, mergers or ventures may prevent or lessen competition while succeeding in realising efficiencies, necessitating a cost-benefit analysis. In other circumstances, of course, neither competition nor efficiency may benefit. The potential "objective" benefits from mergers are often undermined by "subjective" personnel and managerial problems not deriving from "organic" internal growth. Short-term "static" efficiencies may also be counter-balanced in the longer term by "dynamic" inefficiencies from a reduction in flexibility and innovative abilities.

55. A merger represents an investment by the acquiring firm, although it would not directly add to the aggregate stock of investment in the same way as building a new plant would. A merger will often be a speedier and more convenient means of acquiring plant than greenfield investment, while avoiding over-capacity. Such an investment may be particularly beneficial where, for example, the firm taken over is a "failing firm" about to go out of business or where the acquirer is a conglomerate redirecting capital out of an industry with stagnant growth prospects into another industry which is expanding. Further capital injections may follow after the merger, helping to finance new plant or to provide necessary working capital. Mergers may also generate savings from pecuniary economies of scale and rationalization in administration and management. Size and/or diversification may also make a firm better able to raise capital and to reduce interest costs. On the other hand, a take-over may significantly weaken the financial position of the acquiring company (by contrast, a joint venture would be less expensive). A speculative merger may result in the dismemberment of a productive and efficient company. Defensive responses by managers of target companies may be to the detriment of long-term investment, while the profitability and growth of the company which is acquired may also suffer.

56. A number of empirical studies indicate that most mergers are followed by reduced market share growth, profitability, productivity, share valuations, and/or investment[66] (although it is of course difficult to assess whether performance would have been even worse in the absence of the merger). Other studies are inconclusive, or provide evidence of a certain post-merger improvement in market share or investment.[67] Horizontal mergers do appear more likely to be successful than vertical or conglomerate types of mergers. Management buy-outs have a higher chance of success, as they increase the incentive for managers to perform. In general, however, the only parties which have consistently gained from mergers are the shareholders of the acquired firm, since acquiring firms usually pay substantial premiums over quoted share prices. Thus, any efficiency benefits arising from many mergers are often discounted in the purchase price, leaving no net increase (or a decrease) in profitability for the firms involved.

57. An active "market for corporate control" may be a threat to inefficient incumbent management, obliging them to improve the performance of their firms. Where a take-over does occur, it may shift the management of corporate assets to more efficient hands. Cost savings may be generated from rationalization and scale economies in management and administration. On the other hand, the possibility of a take-over may distract the managements of both acquiring and target firms from more productive activity. Where the take-over is consummated, the additional bureaucratic and hierarchical complexity and differences in corporate cultures may complicate the task of management. Such "subjective" difficulties often undermine the potential objective benefits from mergers. One study suggests that the threat of take-over can be an effective spur to efficiency, but that actual take-overs do not lead to efficiency,[68] while it has been suggested that an active "market for corporate control" is a second-best solution for promoting managerial

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66 See for example D. Mueller, *The Determinants and Effects of Mergers - An International Comparison*, Oelgeschlager, Gunn & Hain, Cambridge, Mass., 1980; K. Ravenscraft and F. Scherer, "Mergers, Sell-offs and Economic Efficiency", The Brookings Institution, Washington D.C., 1987; and W. Adams and J. Brock, "The Bigness Mystique and the Merger Policy Debate: An International Perspective", *Northwestern Journal of International Law and Business*, Vol.9, No.1 (1988), p.1.

67 See M. Kumar, *Growth, Acquisition and Investment*, Cambridge, 1984.

68 See P. Holl and J. Pickering, *The Determinants and Effects of Actual, Abandoned and Contested Mergers*, mimeo, University of Manchester, 1986.

accountability and good corporate governance.[69] Joint ventures can be even more difficult to manage than mergers because of lack of clear authority, the transaction costs of co-ordination and conflicting objectives and interests. Non-equity ventures may reduce the commitment of the participants to their success. Such problems are one reason for the instability and brief duration of many joint ventures.

58. Mergers may lead to economies of scale in procurement and transport of production inputs and from increased volume, spreading of fixed costs, expansion of plant, and mechanization at higher levels of output; economies of scope from producing more than one product together; specialization within or among one or more plants, elimination of duplication, reduced downtime, and smaller stocking requirements. Besides these static economies, there can be dynamic economies from the transfer of superior technology and production techniques, or the pooling of resources for their acquisition, and from learning effects associated with increasing experience of production. In horizontal mergers, the importance of such efficiencies will often depend upon the amount of capacity and the rate of growth in the industry concerned. However, many of these efficiencies are inherent to larger plant size - which may not necessarily follow from a merger - rather than larger firm size) Moreover, depending upon the sector, the installation of flexible computer-controlled machinery may either raise or lower minimum economic scale. Thus, production efficiencies have nowadays become increasingly affected by rapid technological and commercial changes. In this respect, smaller firms may generally be better able to withstand demand shocks, since they have greater flexibility.

59. Similarly, while a vertical merger can reduce costs through closer integration of steps in the production chain, reductions in transport costs or uncertainties in supply, or the creation of a two-way channel for information and production skills, in many cases improved communications technologies may make it more efficient to source components from outside and to focus upon core functions in-house. Long-term close co-operation between buyers and suppliers (i.e. "vertical joint ventures") has been a key factor in the competitiveness of many industries.

60. A merger or joint venture can rationalize publicity, marketing, distribution and servicing activities, particularly in exporting. A vertical merger can result in guaranteed markets for sales and secure channels for distribution, although the foreclosure of the production of the supplier firm can reduce its scale economies. However, such efficiencies are not a guaranteed result of mergers and joint ventures. As noted in paragraph 56, the past record of mergers in increasing sales and market share is often not good. Moreover, there is a strong correlation between vigorous domestic rivalry in an industry, even in countries with small domestic markets, and the creation and persistence of competitive advantage in domestic and export markets; this is true not only in fragmented industries but also in those with substantial economies of scale.[70] Such economies are best attained in overseas rather than domestic markets. Few "national champions" are internationally competitive with or without protection and subsidies. However, temporary and conditional infant industry protection, resulting in an oligopoly, may help competitiveness provided strong rivalry persists within the oligopoly, as shown by the experiences of the Republic of Korea.

61. Mergers and joint ventures may lead to efficiency in technological innovation by providing resources, complementarities and economies of scale and scope in research and development (R & D), thus encouraging more ambitious projects and "in-house" technology transfer and reducing the problems of imitation and the social costs of duplicative research efforts. On the other hand, the expense of mergers may reduce research and development spending (the evidence in this respect is conflicting) while, in many circumstances, small firms tend to be more innovative than large firms. Moverover, much of research and development is not characterized by substantial economies of scale.

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69 See "Beyond the merger binge", *Financial Times*, 20 June 1991.

70 See M. Porter, *The Competitive Advantage of Nations*, The MacMilllan Press, London, 1990. See also Utton and Morgan, *op.cit.*.

C. Efficiencies in the context of developing countries

62. There is thus no hard and fast rule that can be stated regarding the relative efficiency advantages or disadvantages of mergers and joint ventures in developing countries. Some guidance as to appropriate cases for mergers in developing countries may be provided by a report by the National Bank of Egypt, which suggests mergers as a possibility where Egyptian enterprises which are otherwise competitive suffer from such problems as lack of optimal size or insufficient cash flow, or from external factors such as stagnation in demand, shortage of foreign exchange for importation of inputs, or unexpected price fluctuations.[71] On the other hand, it is cautioned that mergers would be inappropriate for non-viable enterprises which have exhausted all their assets, or possess huge idle stock because of lack of present or potential future demand, or are unable to compete in export markets; in such cases, liquidation would be the proper solution. Where enterprises are still competitive, it is suggested mergers could be weighed against other solutions such as financial participations, the creation of holding companies to own firms which enjoy managerial independence, or cooperation in marketing activities.

63. The scarcity of resources in developing countries, the importance of economies of scale and scope in the relevant industries and their international competitiveness would need to be taken in to account. Thus, in the Republic of Korea, the high concentration of market power in the hands of the *jaebol* arose because of such factors as scarce entrepreneurial and financial resources and market imperfections, necessitating concentration of entrepreneurship to obtain and utilize production inputs not fully transacted in the market. High concentration has led to a number of efficiency gains. It has resulted in the creation of a few firms that are competitive by world-class standards. Scarce capital resources have been brought together to attain the necessary critical mass necessary in capital-intensive industries. The reputation of the *jaebol* and the artificial inflation of each subsidiary's capital through intercompany shareholdings has facilitated capital raising. Conglomerate structures have enabled cross-subsidization of high risk projects, rotation of scarce skilled personnel, and economies of scope. Production scale economies have also been facilitated; the Republic of Korea's electronics industry, for example, is heavily weighted towards high volume in standardised products subject to sizeable scale economies. A high degree of integration backwards into component production has been an asset, since in-house demand is large and since security of supply of key components has been ensured. *Jaebol* subsidiaries have better bargaining power in technology transfer agreements, resulting in better terms. Efficiencies have also occured in publicity and marketing activities, including through name recognition. Substantial research and development activity has been undertaken. The *jaebol* are behind nearly 40 per cent of total investment, particularly in new technology development.[72] Thus, even in sectors where there has been deregulation, such as the life assurance industry, new market entry has not significantly reduced the dominance of some *jaebol*, due to their reputation, sales ability, efficient management and scale economies.[73]

64. Each of these efficiency gains mentioned above, however, has also had some corollary inefficiencies. Some *jaebol* have at times preferred speculation in real estate to productive investment. The thin capitalization of the *jaebol*, high debts and high diversification into risky industries may have led to financial vulnerability. The financial failure of one *jaebol* subsidiary risks being transmitted to the whole group through inter-company shareholdings, thereby resulting in dangers for the whole economy. The high vertical integration of the *jaebol* has stifled the growth of supplier networks, reliance upon which may be more efficient under current conditions of rapid demand changes and product differentiation (although more outsourcing has now started to take place). The size of the *jaebol* may also deter cooperation with foreign SMEs. The *jaebol* may lack the flexibility and innovative ability to respond to emerging opportunities in frontier technologies. As a result, it has been suggested that the pattern of advance in the Republic of Korea in high technology sectors is likely to be uneven, dependent upon a limited number of large commitments

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71 See National Bank of Egypt, "Mergers of Joint Stock Companies: Economic Considerations and Impact on Ailing Companies", *Economic Bulletin*, pp.135-143, vol. XXXXI, No.3, Cairo (1988).

72 See Sung Taik Han, "Competition Policy and Economic Development in Korea", in *Competition and Economic Development*, p.223.

73 See Un Hoe Park, "Trade in Insurance in Korea", in UNCTAD publication "Services in Asia and the Pacific".

which are uncertain in their outcomes.[74] However, some of the *jaebol* have started to specialize in response to competition from imports, a trend which has been encouraged by the Government, and this may change the picture.

65. In vertical mergers, particular account would need to be taken in developing countries of questions of security and ease of supply, market foreclosure, efficiency of industry structures and the competitiveness of supplier industries *vis-à-vis* imports. The advantages and disadvantages of a high degree of backwards integration in the Republic of Korea have been noted above. Mergers among suppliers can also heighten the vulnerability of the whole industry cluster which they are servicing, or even of the whole economy. Thus, in Australia, where a merger of the two companies which produced springs for cars had been allowed, the whole car industry was brought to a standstill two years later when the company workers went on strike; imports were not competitive because of tariff protection.[75] Pricing is also a key element. In Brazil, vertical integration of manufacturers with inefficient supplier firms, rather than importation of cheaper inputs, may have weakened competitiveness.[76] But vertical integration may sometimes increase competitiveness: in Mexico, for instance, it has been suggested that, since the future strengthening of the patent system is likely to lead to a rapid expansion of foreign investment in the pharmaceuticals sector, the survival strategy of Mexican-owned laboratories should be to form vertically integrated groups through mergers, which would give them a sufficient economic base to acquire new technology and to undertake research.[77] But certain options which could remain open to them include the installation of small multi-purpose laboratories supplying larger producers, and the establishment of export trading companies specialising in products from Mexico's botanical resources. As this example would indicate, acquisitions of control may allow developing country firms to improve their efficiency and competitiveness, but mergers may not necessarily be the only solution to make them more competitive.

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74 See B. Levy and Wen-Jeng Kuo, "The strategic orientation of firms and the performance of Korea and Taiwan in frontier industries : lessons from comparative case studies of keyboard and personal computer assembly", *World Development*, Vol.19, No.4. pp. 363-374, 1991.

75 See the report of "The 3rd Conference on Antitrust Policies in the Asian and Oceanians Countries", Seoul, 1989, p.52.

76 See W. Fritsch and G. Franco, "Efficient industrialisation in a technologically dependent economy: the current Brazilian debate" in *Competition and Economic Development*.

Chapter IV

EFFECTS UPON MARKETS OF DEVELOPING COUNTRIES OF ACQUISITIONS OF CONTROL INVOLVING FOREIGN-CONTROLLED FIRMS

A. Mergers or joint ventures of locally controlled firms with TNC subsidiaries

66. These would not in principle raise different issues regarding market concentration than mergers among locally controlled firms. (The same would be true of mergers among subsidiaries of different TNCs.) However, the usually relatively larger size of TNC subsidiaries, coupled with the fact that they might often be interested in taking over large and/or competitive local firms, may be more likely to lead to market concentration from a merger. It sometimes happens that TNCs buy out "troublesome" local competitors. Thus, in Argentina, a Dutch electronics firms allegedly took over a local competitor to dismantle it.[78] As regards efficiencies, these would not substantially differ from situations where the TNC is a new market entrant, and will be dealt with in the following section. However, it may be noted that an established TNC subsidiary may be likely to use less foreign exchange for take-overs than would an incoming TNC, thus decreasing efficiencies arising from investment. On the other hand the greater local knowledge of an established subsidiary could improve managerial efficiency and the general success of the merger, while production efficiencies and economies can also arise. Where a locally controlled firm takes over a TNC subsidiary, or a management buy-out takes place, reduced TNC involvement would obviously decrease access of the former subsidiary to the "firm-specific assets"[79] of the TNC, but continuing collaboration is common.

B. Mergers/joint ventures of local firms with foreign-based firms

67. A merger or joint venture within a developing country between a locally established firm and a new market entrant, usually a TNC, would not affect market concentration unless the new entity produced wholly or partly for the domestic market, or acted as a trading intermediary. Where this is the case, the new entry may be beneficial by providing a healthy competitive stimulus to concentrated markets, subject to what has been noted previously about the limitations on the extent of competition between TNC subsidiaries and local firms. On the other hand, the new entry may strengthen concentration where the TNC (through imports) and the locally established firm had been competing in the same sector, or would have competed but for the merger or joint venture, i.e. if the TNC would otherwise have begun exporting to the country concerned or would have undertaken a greenfield investment[80] (in practice, of course, it may be difficult to ascertain

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77 See W. P. Nuñez, *Foreign Direct Investment and Industrial Development in Mexico*, OECD Development Centre, Paris, 1990.

78 See consultant study prepared for the UNCTAD secretariat by Mr. E. White.

79 Assets of an intangible nature such as managerial skills, technology, brand names, or marketing networks and know-how.

80 Such a likelihood was the reason why a joint venture in the United States between an American and a Japanese company was invalidated (Brunswick Corp., *et al.*, 94 F.T.C. 1174 (1979), *Aff'd sub nom Yamaha Motor Co.Ltd v. FTC*, 657 F. 2d 971 (8th Circ. 1981)).

what the TNC might have done). The new entry may also lead to future concentration where premature exposure to the superior competitive ability of the TNC leads to the replacement of a local oligopoly by a more efficient foreign controlled oligopoly, as discussed in chapter II. But much would depend upon competition from imports and the competitiveness of local firms; their local knowledge may assist them in some cases.

68. As regards efficiencies, the issues raised by the take-over of a local firm by a foreign firm are similar to those raised by a greenfield investment, but there are some important additional dimensions to be considered. Such a takeover may represent an infusion of investment into the economy, although greenfield investment representing an addition to existing capital stock may be preferable, provided it does not lead to over-capacity, particularly in developing countries where there may be a shortage of alternative investment opportunities and where capital flight may be a possibility. The questions of "additionality" of foreign investment and capital flight have been of concern in relation to debt-equity swaps in particular, since the discount inherent in the swap may subsidize (sometimes with inflationary consequences) investment that would have taken place anyway; however, it appears likely that at least part of the investment undertaken through swaps has been additional.[81] Where finance for a take-over by a foreign firm comes from its local borrowings, this may crowd out local companies and thus have an adverse impact upon local capital formation.

69. To put the question of the provision of investment capital through take-overs by foreign companies into perspective, it may be noted that foreign direct investment as a whole constitutes only a small percentage of gross fixed capital formation in developing countries as a group.[82] However, this should not obscure the fact that, in some developing countries, this percentage is much higher, or that, at the level of individual firms, a take-over by a TNC may sometimes be the only readily available source of investment finance. It may also be noted that there is little evidence that TNCs are any more likely than local firms to "disinvest" and disengage themselves from the local economy. On the other hand, they would often tend to re-invest less of their earnings and remit more funds abroad than local firms[83], although this may depend upon growth prospects. Transfer pricing abuses may also occur.

70. A take-over of a local firm by a TNC would usually lead to the transfer of some "firm-specific assets". Transfers of organizational and managerial skills would be particularly important in view of the growing diffusion of new organizational methods (such as "just-in-time" systems and closer supplier-customer relations) and the large contribution these methods could make to efficiency and productivity in developing country firms. However, these new methods require a lot of managerial and engineering skills. TNCs do train a large percentage of the workers they employ but, in many cases, the transfer of skills is incomplete, particularly in high-level management and engineering functions. On the other hand, TNCs may provide better training in such functions than local firms. Where such a transfer of skills does occur, it may also eventually lead to a diffusion of these skills within the local economy. The above benefits of improved management and organizational skills may, however, be vitiated to some extent by the management difficulties of mergers and joint ventures referred to in paragraph above, which may well be magnified by distance and cultural unfamiliarity. On the other hand, many joint ventures in developing countries work well without such difficulties, perhaps because conflicts of interest among the joint venture partners are not as sharp as in ventures among developed country firms which are potential competitors.

71. A take-over of a local firm by an incoming TNC can give rise to intensive technology transfer to the new subsidiary, often on concessional terms and to a greater extent than would have occured in arms-length transfer arrangements. This would be particularly important in respect of advanced technologies which would otherwise not be transferred. Joint ventures have also led to much technology transfer, although often not to the extent hoped for by local parties. "Strategic alliances" between electronics firms from the Republic of Korea and foreign firms have often been limited in terms of technology transfer, for instance. Whether these benefits will extend to some extent within the industry sector will depend upon technology diffusion by the subsidiary, linkages the TNC maintains with local suppliers (see paragraph 74 below) and the extent to which

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81 See "Transnational banks and debt-equity conversions".

82 See "World Investment Report".

83 See R., Grosse, *Multinationals in Latin America*, London and New York.

emulation by local firms occurs, or employees leave to found their own firms. Contrasting experiences have occurred in different countries in this respect.

72. Where entry into overseas markets is difficult, mergers or joint ventures with foreign firms can overcome entry barriers and provide access to distribution channels, brand names and market knowledge. Not only would a TNC find it easier to penetrate export markets, but it would also be able to make intra-firm sales. On the other hand, there may be market foreclosure through TNCs' internal market allocation arrangements, while under-invoicing could also occur. To the extent that market allocation is compatible with specialization and comparative advantage, efficiency (and structural adjustment at the country level) would be enhanced - although comparative advantage is often created. But what may be efficient in the context of a TNC's worldwide operations may not be efficient for its subsidiary or for the host country. As an OECD study has pointed out, freedom of the component entities of TNCs to act as local profit centres, consistent with the need for specialization and sound commercial practice, could yield significant benefits for international welfare.[84] Where this freedom does not exist, a take-over by a TNC of an efficient local firm involved in exporting may prevent it from attaining optimal exporting capacities.

73. Conflicts of interest in overseas sales can also arise in joint ventures. Thus, in the petrochemical sector, it has been pointed out that reliance by some developing country producers upon joint ventures with major oil companies for marketing in developed countries carries the risk that, in their own interest as producers of the same product, the TNCs concerned will follow non-disruptive marketing strategies which will limit exports, maintain prices and restrict demand.[85] However, tariff and non-tariff barriers and the cost of developing independent marketing channels have so far limited other strategies. By contrast, in the Republic of Korea, firms have favoured self-reliance where possible, and this strategy has sometimes been extremely successful. In the car industry, for instance, the spectacular performance of a *jaebol* car manufacturer which relied upon its own efforts contrasts with the relatively poor performance of a car production joint venture between another *jaebol* and an American manufacturer[86], (which has now been terminated). However, the small size of the domestic market and accelerating technological change have constituted handicaps to the "go-it-alone" strategy.

74. Efficiency in sales would also need to be looked at within the context of the industry cluster within the host country. A TNC subsidiary usually has a higher tendency to source from overseas, including from related firms, than from local suppliers. But extensive local sourcing often takes place where local suppliers are competitive. Moreover, the use of imported inputs may well lead to better export sales of finished products.[87] A key question in individual take-overs by TNCs may therefore be whether, in respect of both inter- and intra-industry sales, any higher propensity to import is likely to be compensated by greater exporting efficiency.

75. In a context of import and foreign investment liberalization, joint ventures with foreign companies may be a means of survival for uncompetitive local companies hitherto selling in protected national markets. In Brazil, for instance, where it is estimated that only 50 out of 360 computer hardware companies are likely to survive following elimination of the "market reserve" restrictions upon foreign computer imports, local firms hope to form joint ventures with TNCs to assemble computers locally or to distribute imported computers, particularly as official approvals for joint ventures will no longer be needed.[4]

76. Mergers and joint ventures between local firms and TNCs may often be beneficial in research and development terms. It is true that TNCs undertake only a small percentage of their total research and development in developing countries, and usually only of a simple character (except in a few countries), while local firms would naturally be more prone to undertaking their research and development locally. In practice, in most developing countries, the research and development

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84 See *Competition and Trade Policies*.

85 See UNIDO, "International Trade and the Marketing of Petrochemicals", *Third Consultation on the Petrochemical Industry*, UNIDO/PC R8, Vienna, November 1985.

86 See C. Oman, "New forms of investment in developing country industries: mining, petrochemicals, automobiles, textiles, food", OECD Development Centre, Paris, 1989, pp.157-160.

87 See "Transnational Corporations and manufactured exports from developing countries".

88 See "Computer MNCs enter Brazil as local market reserve begins to erode", *Business Latin America* p.150, 11 May 1992.

performance of local firms is poor. But, in certain cases, where a local firm taken over by a TNC was efficient and innovative, the take-over may eliminate the possibility of the development of indigenous technological capability; such a consideration would be particularly important since developing countries have limited technological resources. Joint ventures may also lead to over-reliance on the technology provided by the foreign partner and the abandonment of efforts to innovate and adapt the technology to local needs.

77. Overseas mergers or joint ventures undertaken between local and foreign firms would rarely raise competition issues in the domestic markets of developing countries, unless the two firms had previously been competing in export trade to the developing country in question. As noted above, such arrangements are mainly undertaken with a view to obtaining access to technology or overseas markets. While some mergers have been successful in achieving such objectives, others have experienced management, production, marketing or cost problems. Realistically, very few developing country firms would have the means to take over firms in developed countries which are large enough to raise competition concerns.

C. Overseas mergers/joint ventures among foreign firms

78. Some mergers and joint ventures occuring in developed countries in the 1980s, even if they have not had anti-competitive effects in the home countries of the firms involved, have resulted in market concentration in some other countries or at the world level, particularly where they have led to restrictions on the freedom of affiliated firms to compete in certain product or geographical markets. They have also heightened possibilities for collusive arrangements among the fewer firms remaining in different markets. The former Director-General of Fair Trading in the United Kingdom[89] suggested that, while the liberalization of European and international trade has diminished possibilities for cartels to be formed at the national level, the danger that monopolies, cartels and anti-competitive behaviour will re-establish themselves on a European or a wider international level deserves to be taken seriously; in his view, certain industries are particularly prone to international cartelisation, such as those manufacturing industrial commodities where products and prices are uniform, products where production is highly concentrated, products where technological change is slow and products where most producers are TNCs which would otherwise meet in competition across national frontiers.

79. In addition to such sectors, overseas mergers may have a particularly strong impact upon domestic markets of developing countries in their trade channels (because of concentration among trading intermediaries) and in sectors such as some agricultural commodities, some services (because lack of tradeability or of suitable skills in developing countries may limit competition) and high-technology areas. In Pakistan, for example, upon investigation of why the share in tea imports of Kenyan tea had almost trebled in three years while prices were substantially higher than international market prices (even allowing for the high quality of Kenyan tea), the Monopolies Control Authority found that the subsidiaries of two TNCs controlled over half of tea imports (most tea in Pakistan is imported), that their parent companies had been taken over by a third TNC, and that the prices of the tea imported from their Kenyan affiliates were higher than the prices paid to other sellers.[90] After intervention by the Authority, one of the TNCs concerned reduced its shareholding in its Pakistani subsidiary from 50 to 40 per cent.[91] In the airline industry, it has been stated that "many proposed mergers and alliances between leading European airlines look suspiciously like mutual non-agression pacts intended to pre-empt the advent of freer competition by securing dominance in traditional markets".[92] In the auditing service sector, the largest six accounting firms, which have undertaken mergers in recent years, receive 40 per cent of world revenues.[93] Such concentration does not imply a lack of competition; audit fees have

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89 See the "Annual Report of the Director-General of Fair Trading 1988".

90 See "Corporate behaviour in restraint of trade of goods and services in Pakistan", consultant study prepared for the UNCTAD secretariat by Mr. A. Riaz.

91 See "Annual Report of the Monopolies Control Authority", Islamabad, 1991.

92 See "Ventures without frontiers", *Financial Times*, 18 October 1990.

dropped in most countries in the 1980s. But further mergers would certainly raise grounds for concern. The full effects upon developing country markets of many overseas mergers and joint ventures that have taken place during the 1980s will only become apparent during the present decade, as market conditions evolve.

80. It is in high-technology sectors where the effects of overseas mergers may be the most important, since the merging firms are also involved in networks of joint ventures, supply sources are limited, entry barriers such as capital requirements, intellectual property protection and technical standards are often high, and increasing product market segmentation may be limiting substitution possibilities, while developing countries' limited capabilities would usually preclude the build-up of domestic sources. The conditions for obtaining "high-tech" inputs, while relevant to developing countries' import trade and domestic markets, would also often determine competitiveness in export markets. In the biotechnology industry, over 400 seed companies have been bought up, mainly by agro-chemical and food-processing firms (which have themselves undergone a wave of mergers). The plant breeding industry still shows a relatively low-level of concentration, but further consolidation is likely, and the implications for agriculture and medicine remain to be seen.

81. In the semiconductor industry, particularly in Japan, forward linkages with electronic equipment producers, especially computer companies, have helped to smooth out demand fluctuations through "privileged customer" networks, to coordinate design requirements and to improve "speed-to-market";[94] there may also have been cross-subsidization. A corollary of such efficiencies in the performance of these firms, however, is that semiconductor and electronics firms in the Republic of Korea have become dependent for their supply of core components (such as microprocessors) upon the very firms with which they are competing.[95] It is not surprising that inter-firm licensing and joint ventures in the semiconductor industry have declined since the early 1980s, while there is a general reluctance to transfer advanced technology to firms from some Asian countries.[96] Some American firms may also be in such a situation; complaints have been voiced about difficulties in obtaining the latest technology from Japanese companies and about pricing. Within the United States, several antitrust cases involving the computer industry are proceding. It is in this context that grounds for concern may arise from the "solar system" theory of the future of the computer industry, which holds that only two United States and two Japanese computer manufacturers will remain by the end of the century, and the rest will have been pulled into their orbits through mergers.[97] A large number of mergers and joint ventures have in fact recently been taking place in the electronics, computer and semi-conductor industries, no doubt influenced by current recessionary conditions in these sectors. However, any improvement in such conditions will not necessarily lead to new entry, given the height of entry barriers.

82. Of course, it is true that the fluidity of technological change may rapidly reduce market power acquired through mergers and joint ventures. The convergence among telecommunications, electronics and computer sectors also makes it easy for firms from convergent sectors to enter specific product markets. Fierce competition occurs in these sectors at present. Yet such competition among oligopolists may not necessarily extend to all products in all geographic markets, nor may it necessarily take the form of price competition. It has been suggested, for example, that in the telecommunications sector, a joint take-over, by two European firms, of the subsidiary of a third firm, which has enabled the participants to compete better against the market-dominant firm in the European Community as a whole, may have also facilitated collusion with the dominant firm in the French market.[98] Such arrangements are not new; a 1980 report by the European Commission highlights the development of a new form of oligopolistic specialisation at transnational level in which elements of competition are closely bound up with elements of technical or commercial cooperation and quasi-monopolistic rigidity.[99] But recent trends have increased such possibilities. Any adverse effects of market concentration in high-technology sectors may therefore

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93 See T. Noyelle, "Business services and the Uruguay Round negotiations on trade in services", in UNCTAD publication, *Trade in services: Sectoral issues* (UNCTAD ITP/26), 1989.

94 See D. Ernst and D. O'Connor, *Competing in the Electronics Industry - The Experience of Newly Industrialising Economies*, OECD Development Centre (forthcoming).

95 See D. Ernst and D. O'Connor, *Technology and global competition*, OECD Development Centre, Paris, 1989.

96 See "The relevance of recent development in the area of technology to the negotiations on the draft international code of conduct on the transfer of technology" (TD/CODE TOT/55).

97 See "IBM explores PC frontiers", *Financial Times*, 11 July, 1991.

vary among different products and markets, but there would appear to be risks for the domestic markets of developing countries. Such risks would also extend to their export markets and channels. The growing importance and closeness of supplier networks in the electronics/informatics sectors would reinforce the importance for developing country exporters of belonging to these networks. One leading United States semiconductors producer, for example, has reduced the number of suppliers from around 6,000 in 1980 to 1,000 now, out of which 400 are identified as key or preferred suppliers.[100] Distribution networks for computers in Europe and the United States are also currently experiencing a substantial increase in mergers. The entry barriers to exports and distribution in this area make market entry difficult for developing country firms, hence the acquisitions in the distribution sector made by some developing country firms, as noted in paragraph 8 above.

83. The above trends may not necessarily all be to the disadvantage of developing countries. They may help some foreign firms to compete better against other market-dominant firms trading with developing countries. In the past, mergers among retailing chains in developed countries have made it easier for them to establish buying offices in developing countries, thus reducing concentration in export channels. Foreign investment benefits may also flow from a merger. Thus, when a large United States telecommunications company took over a semiconductor subsidiary of another large United States computer company, it also acquired the subsidiary's assembly and test facilities in Thailand and Singapore,[101] and thereupon made massive new investments in these countries. This would suggest that countries which are host to subsidiaries of TNCs may be better off when these TNCs merge or undertake joint ventures than countries which have no such subsidiaries and which may yet be affected in their foreign trade. This would be the case whether the merger or joint venture has positive effects for them, as in the above example, or negative effects, as in the example provided earlier, since remedial action would then be possible.

84. Indeed, where overseas mergers might otherwise have negative effects upon the markets of an individual country, constructive intervention by competition authorities can create positive opportunities. Thus, in a merger of a United States firm with the French subsidiary of another United States firm, an antitrust suit challenging the acquisition of a Californian chemicals plant from the French subsidiary was settled through a divestment of the plant, with an undertaking to help the new owner to set up a research and development laboratory, to advise him on production and to help him to hire and train staff to restore competition in the business.[102] Realistically, however, in many instances, particularly in high-technology areas, TNCs prefer to trade with developing countries rather than to manufacture there. In Germany, cases of purely foreign mergers (i.e. those in which no local subsidiary or at least some production facility exists in Germany) having serious anti-competitive effects in the country, have been rare.[103] But what would be true for a country like Germany may not necessarily be so for most developing countries. Trade and foreign investment liberalization should magnify effects upon developing country markets of overseas mergers among TNCs.

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98 See Commission of the European Communities, "L'évolution de la situation concurrentielle consécutive à certaines fusions dans les secteurs de l'automobile et des télécommunications", Brussels, 1989.

99 See Commission of the European Communities, "Ninth Report on Competition Policy", Brussels, 1980.

100 See Ernst and O' Connor, *op.cit.*.

101 See ESCAP/UNCTC Joint Unit, "Transnational corporations and the electronics industry of ASEAN countries" (UNCTC *Current Studies*, Series A, No.5), 1987.

102 See *International Mergers and Competition Policy*, OECD, Paris, p.38.

103 See "Activities relating to specific provisions of the Set of Principles and Rules" (TD/B/RBP/48).

Chapter V

POLICY FRAMEWORK AFFECTING ACQUISITIONS OF CONTROL

A. General framework

85. A wide range of government policies directly or indirectly affect competition in general and acquisitions of control in particular. These can include policies towards foreign trade, foreign investment, industry and structural adjustment, deregulation, privatization, consumer protection, credit and taxes, and financial market and firm structures. Competition policy should both constitute a key element in the implementation of such policies, and be implemented separately in its own right in the form of competition law controls upon RBPs. There is thus a need for consistency and coherence between those policies and competition law, taking into account the specific objectives of each type of policy and the desirability of competition law being administered in an impartial and independent manner. There is also a need for consistency and neutrality in the application of competition law towards different types of restrictive business practices and acquisitions of control, taking into account their specific effects.

86. Legislation or guidelines governing the functioning of stock markets, and the ownership, share structure, internal regulations and decision-making process of firms all determine the ease with which mergers can be executed, but may also influence competition policy towards mergers. Thus, difficulties in disciplining management may have led to more lenient competition controls upon mergers in the United Sates and the United Kingdom. Developing countries which are now in the process of reforming their structures for capital market and corporate governance would need to take into account not only questions of allocation and ownership of resources, management accountability and efficiency, but also their interplay with competition concerns. Thus, a more active market for corporate control may require more effective competition controls on mergers. Account would also need to be taken in some developing countries of the interplay between market concentration and concentration of corporate ownership. In recognition of this, the Pakistani competition law provides that all undertakings with assets worth over a certain amount must be public companies, while family groups acting through individuals are not allowed to control such companies; excess shareholdings have to be sold off.

87. The merger wave of the 1980s in developed countries was encouraged by the easy availability of finance. Yet, as suggested above, some of the benefits of mergers, particularly the financial benefits, require imperfections in capital markets to exist i.e. large firms have easier and more favourable "access" to capital. In a few developing countries, taking into account such imperfections, government policy has explicitly used financial tools to encourage large firm size or mergers. Thus, the Republic of Korea encouraged the formation and growth of the *jaebol* through tax incentives and concessional credit. However, more bank finance is now being directed towards small and medium-sized enterprises (SMEs), while the *jaebol* are being encouraged to specialize and to divest subsidiaries by giving priority to loans for core activities which they have designated. More easily available finance (as well as more easily available skills and production inputs) in some developing countries may reduce the rationale for mergers. However, given the trend towards financial liberalization and consequently greater difficulties for Governments to direct credit, the risk is always there that large firms will monopolize financial resources. Controls upon mergers and loans in the financial services sector to prevent such monopolization may thus be appropriate, in conjunction with the creation of venture capital facilities for SMEs. Thus the Pakistani competition law controls concessional loans between associated undertakings, particularly if one of them is a bank or insurance company. Conversely, the banking system in developing countries can take a key role in the promotion of mergers where it would be

appropriate, as it is in a good position to assess future trends relating to the economy in general and the firms concerned in particular.[104]

88. As appears from the above, policies relating to mergers and the size of firms are an integral part of industrialization policies in developing countries. Such policies can favour the build-up of large firms through such means as concessional credit, business licensing systems, regulation of industries, or industrial support and incentives, as in the Republic of Korea. Such instruments may also bias firms towards either internal greenfield investment, external expansion (i.e. mergers) or joint ventures. On the other hand, industrialization policies which promote SMEs or provide them with skills, incentives or venture capital can reduce the need for SMEs to seek mergers or joint ventures. Conversely, by "creating competition" and reducing the market power of larger firms, such policies can reduce the need for competition controls on mergers and joint ventures entered into by them.

89. Structural adjustment policies may exempt certain industrial sectors from the application of competition law in order to allow them to rationalize production and to revive the health of industries by, *inter alia*, resorting to mergers and cartels. Flexibility is necessary so as not to impede economic development and efficiency goals, but it may be noted that, although every country exempts certain sectors from competition, competition law can only operate properly if most of the economy is subject to it. In the Republic of Korea, for instance, rationalization programmes for declining "sunset industries" and growing "sunrise industries", which qualify them for government assistance, may only last up to three years; they must, *inter alia*, include plans for necessary cartel activities and (in the case of sunset industries) mergers, while new entry is restricted. The short duration of such government assistance and rationalization programmes and their requirements of efficiency improvements contrast favourably with similar programmes prevailing in other countries. Moreover, the competition law of the Republic of Korea requires other government authorities to consult with the Minister of the Economic Planning Board when they wish to enact any legislation that might restrain competition, although it makes exceptions in the application of competition controls to business integrations likely to substantially restrict competition, particularly in the field of trade, where the aim is to rationalize or to strengthen the international competitiveness of an industry.

90. Deregulation and the removal of regulatory entry barriers, as has occurred in many developing countries, are crucial to ensuring more competition within the economy. As part of this process, state enterprises could be deprived of their monopolies, where appropriate, and subjected to the disciplines of the market and to competition controls (this is done in Chile, for instance). However, the reduction of State intervention requires action to ensure that governmental restrictions and monopolies are not replaced by the private equivalent (unless justified on efficiency grounds). The greater competition ensuing from deregulation has in fact provoked mergers in developed countries (as in the airline industry in the United States or the telecommunications industry in Europe) and should also do so in developing countries, particularly if attempts are made to control the price collusion which has sometimes taken root in the vacuum left by price deregulation. In such circumstances, it would be necessary to apply competition law to ensure that deregulation achieves its objective of benefiting competition and consumer welfare. It is sometimes argued that competition controls are undesirable (because they restrict business activity and market forces) and unnecessary because if, for example, a merger is anti-competitive, market forces will stimulate new entry. However, competition law aims at enhancing the workings of the market by preserving the freedom of enterprises to conduct their businesses unhampered by restrictions imposed by other enterprises. Nor can it be assumed that entry barriers or other market imperfections will invariably be easily or quickly overcome by potential competitors. Of course, merger controls following deregulation should be applied selectively so as not to inhibit desirable restructuring.

91. Privatization is an essential part of the process of deregulation and the withdrawal of Governments from direct economic intervention. Although privatizations resemble mergers in some respect, since they involve a change in the ownership of enterprises, merger controls may not necessarily be an appropriate instrument to ensure that public monopolies are not replaced by the private equivalent; "internal" consultations between competition authorities and authorities responsible for privatization may sometimes be more useful. However, to prepare for a

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[104] This has been suggested in Egypt; see National Bank of Egypt, *op.cit.*

privatization, competition authorities might undertake an analysis of the market in a manner similar to the analysis applied to mergers. Competition considerations could be taken into account in the privatization process by, as appropriate, splitting up the enterprise to be privatized, utilizing the optimum method for privatization (from the competition point of view), or choosing a buyer who does not already have a dominant position in the market, particularly as, after a privatization has taken place, the monitoring of the competitive behaviour of the enterprise concerned is likely to be an ongoing task for the RBP control authorities.

92. Competition policy and consumer protection are basically complementary. Competition policy seeks to preserve and encourage competition to the benefit of consumers. Consumer protection policy regulates prices (although, where possible, competition is the best "regulator" of prices), or provides consumers with information and redress mechanisms to ensure that the competitive process works effectively. It may sometimes happen, however, that competition and consumer protection policies conflict. Business licensing systems, prudential controls, or price controls can discourage market entry. In such cases, a cost/benefit analysis would be necessary, and where the decision is taken to maintain such controls, they should be taken into account in analysing the likely effects of acquisitions of control.

93. As international mergers and joint ventures are types of foreign investment, they may be subject in many countries to investment controls and performance requirements; they may also be granted incentives. Given this, and given that the foreign investment régimes of developing countries are being liberalized, consistency and co-ordination in the implementation of their competition and foreign investment laws are important. Account could be taken in this respect of other countries' experiences. In Czechoslovkia, a controversy has arisen as to whether, in taking over a state-owned car company being privatized, a German car company was promised immunity from the application of the competition law to the transaction; the controversy has been sharpened by a subsequent substantial price increase.[105] In Canada, the agency responsible for the review of foreign investment, Investment Canada, looks at the broad question of net benefits to Canada from the investment, including the impact on competition. While the Bureau of Competition Policy advises on the assessment of this impact, the two agencies and their processes are separate and independent, and are not bound by each other's decisions. It may also be noted that, in some developed countries, there are foreign investment restrictions on takeovers by foreign firms in a few sectors.

94. In the interface between competition and trade, the temporary benefits to local producers of regulatory barriers against imports would need to be weighed against the potential advantages for local consumers of trade liberalization. "Infant industry" protection may be justified, but inappropriate or over-lengthy shielding of domestic enterprises from competition from imports can lead to the creation of "permanent infants", benefiting neither producers nor consumers. To the extent that imports are restricted, the need to preserve competitive market structures within the country is even greater, but, as noted above, despite trade liberalization, complementary competition action may be required.

95. Whether the policy decision taken is to favour national producers or consumers, it would appear advisable to maintain a certain degree of consistency. In the United Kingdom, where enquiries by the Office of Fair Trading regarding the domestic soda ash industry led to the relaxation of customer contract terms with a view to opening the market to foreign competition, it has been suggested that the later imposition of anti-dumping duties on soda ash from the United States by the European Commission might be linked to the fact that the Commission subsequently had to investigate a cartel within the Community's concentrated soda ash industry.[106] (The cartel has since been fined, and the anti-dumping measures terminated.) It has been suggested that there is an inconsistency between demands made during the Structural Impediment Initiative (SII) talks that cartels in Japan be eliminated, and arrangements for VERs for different imported products, as well as market share targets for semiconductor exports, which may necessitate cartels to put them into effect.[107]

96. Trade and competition policies may, of course, aim at different objectives. Thus, in a deci-

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[105] See "Czech, Slovak federal officials examine impact of Skoda/VW merger", *Antitrust and Trade Regulation Report*, Vol.62, p.364, 19 March 1992.

[106] See "Annual Report of the Director-General of Fair Trading, 1988", Her Majesty's Stationery Office, London, 1988.

[107] See "Assault on Japan", *Financial Times*, 10 June 1991.

sion in the United States on an appeal from an anti-dumping case decided by the International Trade Commission, the court overruled the finding that steel imports from Argentina did not injure or threaten injury to the United States industry, rejecting an analysis which had taken into account the presence or absence of barriers to entry of other imports.[108] While such barriers would be relevant in looking at "injury to competition", the anti-dumping statute was concerned with "injury to industry", reflecting the legislative judgement that this might be severe enough to justify relief even if the economy as a whole might be better served without such relief.

97. On the other hand, competition law measures can replace trade measures. Thus, the Australia-New Zealand Free Trade Agreement Protocol on the Acceleration of Free Trade in Goods commits these two countries to relying upon competition laws rather than anti-dumping laws in respect of their bilateral trade in goods. Competition law issues can also be taken into account in the application of anti-dumping measures. Thus, the European Court of Justice has recently ruled, in an appeal relating to anti-dumping measures taken against imports of calcium metal from China and the former Soviet Union, that in assessing damage suffered by EEC industry, only the injury caused by dumped imports must be taken into account and that injury caused by other factors, including anti-competitive conduct by the EEC industry itself (a single French corporation), must not be attributed to dumped imports.[109]

98. Competition law can take into account conduct occurring overseas in the decision as to whether or not to take action against horizontal arrangements affecting imports. Joint buying pools to countervail the power of foreign suppliers regulate, for instance, the importation of sulphuric acid into the United Kingdom, or sulphur in Australia, and are exempted from competition law. However, competition proceedings can be taken against such buying pools in some exporting countries; United States competition law has been enforced against import cartels set up overseas to countervail the market power of Webb-Pomerene associations.[110]

99. Competition law can also be applied in respect of export trade. The United States Justice Department has recently issued a policy statement re-extending the possibility of antitrust enforcement action by the Department to conduct occurring overseas that restrains United States exports, whether or not there is direct harm to domestic customers, provided the effect upon exports is direct, substantial and reasonably foreseeable, there are anti-competitive activities violating United States laws, and United States courts have personal jurisdiction.[111] Conversely, United States trade legislation provides that trade action can be taken against any goods from a country that injures United States trading interests by the purposeful non-enforcement of its anti-trust laws.[112]

100. The above review of the links between competition and trade policies would suggest that such links are becoming ever closer. This does not mean that the two sets of policies are being, or should be, merged; each has its distinct rationale and purpose. Yet suggestions are being made that a multilateral normative framework may be useful to recognize and structure the links between competition and trade policies, to take into account the increasingly global context for the implementation of competition policy, and to ensure the continuing development of the international trading system, as conceived in the Havana Charter. Thus, Sir Leon Brittan, head of the European Commission's Directorate-General for Competition, has suggested that GATT rules be examined to see how they could be applied to competition policy to develop minimum rules and enforcement standards to be respected by Governments.[113] Sir Leon has noted that as a result of the growing interdependence of the world economy, domestic competition policies can distort trade, and that EEC companies subject to strict competition policies could be placed at a disadvantage *vis-à-vis* companies based in countries where such policies are non-existent or are not enforced. Indeed, Japanese officials are reported to have expressed the opinion that any United States antitrust action against foreign firms' conduct on the grounds that it injures American

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108 See USX Corp. v. United States International Trade Commission, 628F Suppl.60.

109 Case C-358/89, Extramet Industrie SA v.Council, 6CH, 11 June 1992.

110 See Daishowa International v. North Coast Export Co., 1982-2, Trade Cas. (CCH) 64, 771 (1982).

111 See *Department of Justice Press Release* No. 92-117 of 3 April 1992.

112 See section 301 of the Omnibus Trading and Competitiveness Act, 1990.

113 See "Brittan urges role for GATT in competition enforcement", *Financial Times*, 3 February 1992, and "EC Commissioner urges examination of global antitrust rules", *Antitrust and Trade Regulation Report*, Vol.62, p.357, 19 March 1992.

exporters would violate GATT codes.[114] Legislation is in fact being considered by the United States Congress requiring the President to enter into negotiations to conclude trade agreements that would (a) eliminate the adverse effects of private anticompetitive practices, harmonize competition laws and their implementation, and establish mechanisms for their effective enforcement across national boundaries, insofar as these practices or laws relate to international trade; and (b) make the GATT compatible with these new agreements and with United States antitrust law.[115]

101. In this connection, it may be recalled that Article E.4 of the Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices (the RBPs Set) provides that States should seek appropriate remedial or preventive measures to prevent and/or control the use of restrictive business practices within their competence when it comes to their attention that such practices adversely affect international trade, and particularly the trade and development of the developing countries. The implementation of this provision would be a step towards any elaboration of strengthened multilateral norms linking competition and trade.

B. Competition law framework

102. Competition law control of clauses in horizontal and vertical licensing, distribution and other arrangements is necessarily interrelated with enforcement policy towards mergers and joint ventures. Many practices between independent firms are proscribed, or would be subject to screening, while the same practices in the context of an economic entitity under common control would escape scrutiny. If firms are not to be encouraged to escape the regulation of such practices by joining together, consistency would require a control over mergers which is no less strict than that applied to concerted practices. Throughout the 1980s, controls over practices in licensing arrangements have been liberalized, particularly in the context of "vertical" relationships, but are often still subject to scrutiny. The possibilities for merging firms to undertake such practices once they are under common control would indicate a strong need to verify that mergers which lead to concentration of market power also genuinely result in pro-competitive efficiencies.

103. Of course, enterprises wishing to undertake mergers for legitimate reasons relating to business organisation or investment cannot be subject to sanctions, as would those conspiring to fix prices, for instance. Moreover, market power accruing as a result of changes in market structure may not necessarily be abused while, if abuse does occur, remedies may be available. Yet competition law is more concerned with the likely effects upon competition rather than the possible motivations of business arrangements, while the practical difficulties of detecting post-merger abuse, the elimination of alternative sources of supply for the consumer, or the possibility that other firms in the market will avoid competing too strongly with the market-dominant firm would normally make it preferable to avoid the creation of market dominance in the first place.

104. Market dominance or monopoly may arise in ways other than through acquisitions of control, through the normal competitive process or through market exit by other firms, for instance. Competition laws therefore pay attention to "static" existing concentration of market power as well as "dynamic" situations. Competitive success is not in itself penalised, but possibilities of abuse arising from market dominance are looked at closely. In developing countries with concentrated market structures, as much if not more attention would need to be paid to existing monopolies or oligopolies as to concentration arising through acquisitions of control. However, it would be preferable, where possible, to reduce market concentration by promotional or incentive measures aimed at SMEs and by pre-emptive measures against anti-competitive mergers, rather than by *ex post* measures against monopolies.

105. Competition law can in fact attempt to control internal growth in the same manner as external growth. Thus, the Republic of Korea's competition law controls the establishment of new enterprises by market-dominating firms in the same manner as mergers. The Indian law went even

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[114] See "Japanese trade ministry to study plea by U.S. to extend reach of antitrust law", *Antitrust and Trade Regulation Report*, Vol.62, p.479, 9 April 1992.

[115] See Press Release of 17 June 1992, Committee of Ways and Means, United States House of Representatives.

further by controlling any substantial expansion of the activities of an undertaking which had assets of a certain worth, or which was a dominant undertaking (see paragraph 131 below). However, the implementation of this law has now been liberalized. If countries choose to control internal growth, full weight should at least be given to efficiency considerations.

106. In the relative application of competition law towards mergers and joint ventures, it has been suggested that broadly similar economic analyses and enforcement techniques be applied by competition authorities; otherwise, if more relaxed rules are applied to mergers than to research and development joint ventures, for instance, two companies may be forced to merge when a less formal agreement would better meet their needs and the economic goals of society.[116] It has therefore been recommended that public policy take a neutral stance between mergers and other forms of business organization (joint ventures, licensing and greenfield investment).

107. At the present time, in developed countries, most categories of joint ventures - apart from naked cartels - are probably subjected to substantially similar economic analysis as mergers. Yet disparities still exist in the substantive law and the administrative mechanisms applicable to mergers and to different types of joint ventures. Even differences in the speed with which different business arrangements are considered by the competition authorities can distort the form of such arrangments. Anecdotal evidence would indicate, for instance, that firms in the European Community entering into large joint ventures attempt to structure them in such a way that they would be considered "concentrative" rather than "cooperative" ventures, thus falling under the new merger control regulation and being dealt more speedily.[117] The differences between the two types of ventures hinge upon such factors a s joint control, autonomy and the withdrawal of the parents from the relevant market. However, measures aimed at reducing the differences in the treatment of cooperative and concentrative joint ventures are being considered by the Commission.

108. Of course, there may be good reasons why differential treatment is accorded to different business arrangements. The *per se* condemnation traditionally reserved for cartels has no doubt been a major reason why joint ventures have been covered by different competition law provisions from those covering mergers, despite the fact that the dividing line between mergers and joint ventures is sometimes thin (such as where, for example, there is a joint acquisition by two companies of a third company). Some degree of cartelisation may indeed be inherent in some types of joint ventures which increase efficiency. In developing countries, joint ventures with foreign partners have usually been accorded much more favourable treatment than mergers, so as to obtain the benefits of close relations with a foreign firm while maintaining a degree of independence for the local party; differential treatment has also sometimes been accorded to contractual and equity joint ventures. In many cases, however, even a minority joint venture stake has sufficed to ensure effective control by the foreign party, while the expected benefits of joint ventures have often been elusive.

109. Some reconsideration and refinement of relative policies towards different types of joint ventures and mergers may therefore be appropriate. The review in the following chapter will mainly concentrate on competition policy towards mergers, but with some reference to joint ventures, as well as interlocking shareholdings or directorates.

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116 See speech delivered at Fordham University on 19 October 1990 by the Director of Investigation and Research of the Canadian Bureau of Competition Policy. Reported in the Canadian Competition Policy Record.

117 See *Council Regulation (EEC)* No 4064/89 of 21 December 1989 *on the control of concentration* between undertakings and Commission Notice regarding the concentrative and cooperative operations under *Council Regulation (EEC)*, No. 4064/89 O.J.L 365.1 (1989) as amended, *Official Journal*, L 295/14 (1990).

Chapter VI

COMPETITION RULES AND EXPERIENCES RELATING TO MERGERS

A. Developed countries

110. In recent years, a number of developed countries, including Belgium, Greece, Italy, Norway, Portugal, Spain, Sweden and Switzerland, as well as the European Commission, have adopted merger control legislation for the first time, although to some extent they may already have been subjecting mergers to their competition controls upon abuses of dominant position and monopolies. Other countries such as Australia, Canada, France, Germany, Ireland, New Zealand and the United States have made significant changes to their merger control laws or policies. Further changes by a few countries are pending. The legislative activity in this area, as well as often stronger enforcement activity, indicates the high degree of importance attached to merger control in developed countries. It is true that in the 1980s there was a liberalization, in overall terms relative to earlier strict merger controls, of federal merger enforcement in the United States,[118] but this has not necessarily occurred in the case-by-case assessment of individual mergers. Moreover, enforcement policies in some states of the United States are stricter than at the federal level, while the courts have taken an independent line.

111. Important differences continue to exist in the competition laws and enforcement policies on mergers of different developed countries in respect, *inter alia*, of: the definition of a merger; market definition; the anti-competitive threshold to be attained; market share thresholds; the relative importance of structural and behavioural factors; the relative importance of risks of dominance and collusion; the considerations to be taken into account other than market concentration; the treatment of vertical and conglomerate mergers; the treatment of efficiency gains; the application of the "failing firm" defence; the coverage and structure of exemptions; institutional arrangements; and a number of procedures. However, the similarities among competition regimes of developed countries are far more important than the differences. Their basic objectives are substantially similar, and their primary concerns relate to market power being exercised over prices, or other dimensions of competition.

112. In recent years, the general tendency in developed countries, in the assessment of the likely effects of mergers, has been to rely relatively more upon economic analysis taking into account behavioural factors and possibilities for substitution and new entry, and relatively less upon market share data and market structure effects in a static perspective. However, much weight is still assigned to "structuralist" considerations. The application of economic analysis has contributed, *inter alia*, to greater account being taken of the increasing internationalization and interdependence of markets. The review undertaken below of the legislation and enforcement policies of developed countries will focus mainly on how this question, as well as questions of efficiency and "competitiveness", are dealt with.

113. The basic criterion for determining harm to competition varies from the substantial lessening of competition or tendency to create a monopoly (as in the United States) to the creation or strengthening of market domination if not outweighed by improvements in competitive conditions (as in Germany) or to a broad public interest test (as in the United Kingdom), where competition is one among a number of other criteria, including the effects of a merger in "maintaining and promoting competitive activity in overseas markets by United Kingdom

[118] See "GAO reports huge decline in enforcement by Antitrust Division during Reagan era", *Antitrust and Trade Regulation Report*, Vol.59, p.861, 13 December 1990.

firms".[119] But, in practice, the differences among these different criteria are not great. In countries using a public interest criterion, enforcement policy usually attaches greater weight to competition than to other factors. In the United Kingdom, for instance,the Tebbitt Guidelines clarify that mergers will be challenged mainly, but not exclusively, upon competition grounds.[120] It may be noted that the former Director-General of Fair Trading has proposed that the burden of proof to show efficiency gains arising from potentially anti-competitive mergers should rest upon the firms involved, thus effectively tightening merger controls.[121]

114. In Germany, the competition authorities do not consider questions of competitiveness in overseas markets, but do take into account the achievement of efficiencies at the firm level if they have a beneficial impact upon the structure of a market, thereby leading to an improvement of competitive conditions. However, the Federal Minister for Economic Affairs may authorize a merger if its restraint upon competition is outweighed by advantages to the whole economy from the merger, or if it is justified by a predominating public interest.[122] This political review process may take into account the competitiveness of the participating enterprises outside the area of application of the competition law, but the authorization may only be granted if the extent of the restraint does not endanger the market economy system. In practice, although decisions of the Federal Cartel Office have been occasionally overridden by the Minister (as in the famous Daimler-Benz/MBB merger), this has not occurred very often.

115. In the United States, efficiencies are not a cognizable defence to a merger having anti-competitive effects, but are taken into account by federal enforcement agencies as one of the factors in deciding whether or not to oppose a merger (the wording of the 1992 Merger Guidelines [123] appears to relax the burden of proof of efficiences as compared with the previous 1984 Guidelines). Claims of efficiencies will be rejected if other means exist to attain them, and the expected net efficiencies must be greater the more significant the competitive risks. However, competitiveness considerations are not taken into account, given the strong consumer welfare focus of United States competition law. The merger enforcement guidelines do note that efficiency can "increase the competitiveness of firms and result in lower prices to the consumer",[124] while the promotion of international competitiveness is accepted as a pro-competitive element in respect of research and development joint ventures.[125] Moreover, as noted above, a Justice Department statement of 3 April 1992 re-extends the possibility of antitrust enforcement action to conduct occurring overseas that restrains United States exports, whether or not there is direct harm to United States consumers.

116. The new European Economic Community merger regulations allow, as well as actual or potential competition from undertakings located within or outside the Community, the development of "technical and economic progress" to be taken into account "provided it is to consumers' advantage and does not form an obstacle to competition". It has been stated that such progress is not a legitimate defence for a merger which creates a dominant position; in any event, economic progress could not exist in an uncompetitive market since it would be confined to the dominant company itself,[126] while a competitive world market would not justify a dominant position within the Community. Yet the recent controversy within the European Community over the vetoing by the European Commission of the proposed take-over by Aérospatiale and Aliéna, a French and an Italian aviation company, of de Havilland, a Canadian company, and ongoing discussions about changes in the Commission's merger review machinery, show that the tensions between "pure" competition questions and considerations of industrial policy and competitiveness are far from resolved.

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[119] See Section 84 of the Fair Trading Act 1973.

[120] See the House of Commons written answer by the Secretary of State for Trade and Industry, of 5 July 1984 (the "Tebbitt guidelines").

[121] See "Enemy of restrictive practices", Financial Times, 23 March 1992.

[122] See section 24 (3) of the Act against Restraints of Competition of 27 July 1957.

[123] See the Department of Justice and Federal Trade Commission, *Horizontal Merger Guidelines*, 2 April 1992 (the 1992 Guidelines).

[124] See paragraph 4 of the 1992 *Guidelines*.

[125] See the National Co-operative Research Act of 1984.

[126] See Sir Leon Brittan, "The Law and Policy of Merger Control in the EEC", *European Law Review*, October 1990, p.353.

117. It is in Canada where questions of competitiveness and efficiency are taken into account most strongly and explicitly.[127] In the evaluation of a merger's anti-competitive effects, the extent to which there is likely to be significant competition from foreign firms is taken into account. Mergers have to be allowed if they bring about gains in efficiency that will be greater than and will offset the effects of any prevention or lessening of competition, when such gains would not otherwise be attained; it must be considered if such gains will result in a significant increase in the real value of exports or substitution of domestic for imported products. Efficiency gains must offset the loss arising from an exercise of market power, but not the expropriation of consumer surplus by producers.[128] Thus, unlike American law, Canadian enforcement policy aims at the maximization of total social welfare rather than of consumer welfare. The Canadian enforcement guidelines note that the assessment of foreign competition is particularly important in the context of the globalization of markets, the continuing growth in foreign direct investment and strategic alliances in Canada, the free trade agreement with the United States, the rationalization of European industry facilitated by European Community integration and vigorous competition from firms in newly industrialized countries.

118. However, in general, competition rather than competitiveness is usually the decisive criterion in the bulk of merger cases considered in developed countries. Moreover, larger size is not automatically assumed to lead to greater competitiveness, while alternative means of strengthening efficiency and competitiveness are taken into account. Yet increasing economic globalization would suggest that the issue of the extent to which there is a conflict between competition and competitiveness is likely to become ever more controversial (as indicated by the controversy noted above in the de Havilland case), as policy-makers are faced with the dilemma of whether to allow mergers among local firms so as to enable them (possibly) to better compete against foreign enterprises, or to prevent such mergers so as to avoid the risk of anti-competitive behaviour.

119. It is of course common, in most jurisdictions, as part of the process of defining the relevant geographical market or of assessing existing competition or likely market entry, to take account of both existing competition from imported goods and the possibilities for foreign firms to increase their exports to the country concerned in response to an attempt to exercise market power by merging firms. Even in this respect, however, competition authorities would need to decide upon the weight to be assigned to imports. Thus, while the German enforcement guidelines consider that the market position of present foreign competitors has "to be determined on the basis of their actual domestic shipments or sales" and that "potential foreign competition as a rule is of very limited importance to domestic markets because the likelihood of market entry cannot be established with sufficient certainty",[129] under United States federal enforcement policy, "existing foreign competitors are not excluded from a relevant market solely because their sales in the United States are subject to quotas or other governmentally-imposed trade restrictions... because it is difficult to assess the effectiveness or longevity of such restraints and to measure the likely offsetting supply responses"; the restraint in question has to be "effective" and "binding".[130]

120. In this connection, it may be recalled that most countries, as a matter of policy, only control market structures or conduct which produce anticompetitive effects on the domestic market, and make no attempt to deal with any adverse effects on the import trade or domestic markets of foreign countries. Specific statutory exemptions from the application of competition law are provided to export joint ventures or cartels in several countries although "spillover" effects of export cartels upon competition in domestic markets would usually be subject to scrutiny. In some countries, the exemption only applies if formal notification or registration of the export agreement is made to the competition authorities. Confidentiality is usually maintained regarding cartels even if they have been notified or registered. The fact that production is being more and more undertaken in a specialized manner on an international scale suggests that "spillover" onto domestic markets, although probably still relatively infrequent, is likely to happen increasingly often, as production inputs exported from some countries are used for manufacture in other

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[127] See the Competition Act of 1986.

[128] See "Merger Enforcement Guidelines", Director of Investigation and Research, Ottawa, March 1991.

[129] See "Marktbeherrschung in der Fusion Kontrolle: Checklist for Merger Control Procedures", paragraph 7, Berlin, 1990. See also the 1985/86 Activity Report of the Federal Cartel Office, paragraphs 2 and 6.

[130] See "US Department of Justice Antitrust Enforcement Guidelines for International Operations", November 1988, paragraph 3323. See also the Merger Guidelines of 1992.

countries and then come back in finished form. This casts doubts about the future tenability of sharp distinctions between effects upon domestic and foreign markets. Morever, as noted above, export cartels can breed countervailing import cartels. But competition law enforcement has yet to get fully to grips with such issues.

121. Under the principle of territoriality, all developed countries apply their laws to conduct that takes place within their national territory, regardless of the nationality of the persons involved. "Objective" territorial jurisdiction is also asserted by some countries, under certain conditions upon, acts starting abroad and ending in national territory. In addition, the concept of "enterprise unity" has been sometimes used to establish personal jurisdiction over foreign-based parents where they exercise the requisite degree of control over local affiliates.[131] More controversially, enterprise unity has also been applied in some countries to hold domestic parents or subsidiaries responsible for the conduct of their affiliates abroad.[132] Other controversies have arisen in the past from the application of United States law providing that actions by foreign subsidiaries of American companies would, in accordance with the nationality principle, fall within American jurisdiction.

122. However, the main controversies that have arisen in the past relate to the application of the "effects doctrine" by the United States, under which subject matter jurisdiction is asserted with respect to any anti-competitive practices by foreign parties abroad having effects on the American market or export trade, as occurred in the uranium cartel cases of the late 1970s. The effects doctrine has not often been applied to mergers of foreign companies; such mergers have sometimes been allowed on conditions linked to the divestment of United States subsidiaries [133] or to the leasing of part of the business of the acquired company and undertakings concerning future acquisitions,[134] but have also been prevented on occasion.[135] Action has been taken even where subsidiaries or substantial assets are not present within the United States, as occurred in the Institut Mérieux case.

123. The application of the "effects doctrine" under United States law is tempered by "comity" considerations which lead to a balancing of relative national and foreign interests, or a limited abstention of exercise of jurisdiction based on diplomatic suggestions and considerations.[136] However, there are ambiguities and discrepancies in the relevant case law. The Department of Justice's enforcement policy (under the 1988 Guidelines) is to consider whether significant interests of any foreign sovereign would be affected and to assert jurisdiction only when it is concluded that it would be reasonable to do so, taking into account, *inter alia*, whether effective relief could be obtained. This would not of course deter private action, as in the Minorco case; private suits constitute the bulk of antitrust cases in the United States. In a private action by American plaintiffs against British re-insurance firms relating to conduct on the London re-insurance market, the case was initially dismissed on the grounds of "international comity", but was successful on appeal, as it was concluded that the "significant conflict with English law and policy" was outweighed by other factors [137] (briefs were filed by the British and United States Governments respectively opposing and supporting the case). Other tempering factors include the foreign sovereign immunity, act of State, and foreign sovereign compulsion defences. However, the scope of these defences under United States law is not entirely clear.

124. In Germany, the competition law applies to "all restraints of competition which have effect" within German territory, "even if they result from acts done outside".[138] Thus, the Supreme Court has ruled that pre-notification requirements can extend to an overseas merger of foreign enterprises without local subsidiaries, if they produce perceptible and direct domestic effects on the German

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131 See for example Case 48/69, Imperial Chemical Industries Ltd. v. European Commission; Case 52/69, J.R. Geigy v. Commission; Case 53/69, Sandoz v. Commission, 1972, E.C.R. 619, 787, 845.

132 See for example the United States Supreme Court case of *Continental Ore Co. v. Union Carbide and Carbon Co.*, 370 U.S. 690 (1962).

133 See *United States v. CIBA Corp.*,(1970) Trade Cas. (CCH) 73, 269 (S.D.N.Y. 1970).

134 *Institut Mérieux, S.A.*, No. 891,0098; 55 Fed. Reg. 1614 (17 January 1990).

135 See *Consolidated Gold Fields PLC v. Minorco, S.A.* 871 F. 2d 253 (2d Cir. 1989).

136 See, in particular, *Timberland Lumber Co. v. Bank of America*, 549 F. 2d 597 (9th Cir. 1976) and *Mannington Mills v. Congoleum Corp.*,595 F. 2d 1287 (3rd Cir. 1979).

137 In re *Insurance Antitrust Litigation 723F.* Supp 464 (N.D.Ca.1989), 938 F.2d 919 (9th Cir. 1991).

138 See section 98(2) of the Act against Restraints of Competition of 27 July 1957.

market.[139] However, in another case, a prohibition of an overseas merger between non-German parties was over-ruled on the basis that the public international law principles of reasonable forum contacts and non-interference had been violated; the merger's "centre of gravity" was overseas, the increase of market power on the domestic market was relatively insignificant, and the merger had been approved by the French authorities.[140] In another case where an overseas merger had concrete effects on the domestic market, it was ruled that only that part of the merger having domestic effects (i.e. the merger of the local subsidiaries) should be prohibited; the prohibition of the whole merger was annulled on the basis of conflict with the non-interference and reasonable contacts principles.[141]

125. Recently adopted or revised competition laws of EEC countries all proscribe agreements, including agreements formed overseas, that have as their object or effect the distortion of competition on the national markets and the abuse of a dominant position. This has been applied in appropriate cases in France, for example.[142] European Community institutions rely upon the "objective" territoriality principle to assert jurisdiction over agreements formed abroad and implemented within the EEC, irrespective of whether or not there is recourse to EEC subsidiaries to make contacts with EEC purchasers (as in the famous Wood Pulp case).[143] The Merger Regulation appplies to mergers of non-EEC companies on the basis of a minimum turnover in the EEC, irrespective of whether there is physical presence therein (a number of overseas mergers among foreign companies have been screened.)

126. Despite the legal differences between "effects" and objective territorial jurisdiction, it appears that, in practical terms, their application would often yield the same results, and this may decrease possibilities for conflicts among Governments. Yet certain practices by foreign firms like concerted refusals of supply to importers or import cartels, or mergers between foreign firms exporting to a country where they have no subsidiaries or assets, might well fall outside substantive territorial jurisdiction, but be caught under "effects" jurisdiction. Also relevant to differences in the treatment of such situations are: the scope of personal jurisdiction, of the doctrine of enterprise unity, and of the nationality principle; the willingness to take into consideration effects upon export trade; the lack of clarity relating to the scope of legal or enforcement principles which would take foreign interests into account, and differences among countries as to which principles would be applied and the scope of their application; the willingness to intervene when effective relief depends upon action outside national territory; and the frequency with which private actions (which would be less mindful of comity considerations) are initiated.

127. Indeed, the very fact that the application of "objective" territorial jurisdiction would often lead to the same results as that of "effects" jurisdiction suggests that jurisdictional conflicts may, in future, become sharper than they have been in recent years. Already, several mergers or joint ventures have required approval by more than one competition authority, with one authority approving and another disapproving of, or imposing conditions upon, a merger. Most notably, a merger between two major razor and blade companies has been reviewed by seven competition authorities; divestment orders have been made in the United Kingdom [144] and France [145] and a rescission enforced in respect of the United States part of the transaction.[146] Such multiple merger reviews may lead to different substantive results where there are different competitive effects in different countries or divergences in regulatory objectives or in substantive criteria. Procedural problems could also arise, particularly with respect to multiple and differing pre-notification and information requirements and deadlines.

128. In fact, as noted above, controversies in the area of competition have arisen in the past, mainly in respect of attempts by the United States to obtain evidence, to serve process or to en-

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139 The *Organic Pigments case* (1979) E.C.C. 533.

140 The *Bayer/Firestone* case KG Nr. 26 1980 WuW/E OLG, 2419 (Synthetischer Kautschuk II).

141 See the *Philip Morris/Rothmans* case, 29 October 1985, WuW 6/1986, pp.481-495.

142 See F. Souty, "Théorie de l'effet: les entreprises des pays tiers et le respect de la concurrence sur le marché européen", Revue de la concurrence et de la consommation, No. 65, p.6, Janv.-Fév. 1992.

143 See *Ahlström et al. v. European Commission*, (1988) ECR 5193, (1988) 4 C.M.L.R. 901).

144 See "Gillette given 6 months to divest Eemland interests", *Financial Times*, 13 March 1992.

145 See "French government bans deal in razor and blade markets", Antitrust and Trade Regulation Report, Vol. 362, p. 361, 19 March 1992.

146 See *United States v. Gillette Co.*, 1990-2, Trade Cas (CCH) 69, 142 (D.D.C. 25 July 1980).

force judgements in antitrust cases relating to conduct occurring overseas having anti-competitive effects on the United States market; several developed countries have adopted "blocking" statutes providing the authority to prevent such attempts within their territory. Such controversies have died down as a result of greater attention to comity considerations and cooperation undertaken by competition authorities of developed countries. Such cooperation efforts are dealt with in section C of this chapter, where an assessment is made of whether the current status quo is entirely satisfactory.

B. Developing countries

129. A number of developing countries from all regions have adopted competition laws,[147] some of them dealing specifically with mergers and others applying indirectly to mergers through provisions against abuse of dominant positions, monopolies, or impediments against free competition. Some of these laws are quite old: Brazil's law, for instance, dates back to 1962,[148] (although it has recently been substantially reformed),[149] while India's law dates back to 1969 [150] and Pakistan's to 1971.[151] Others are quite recent, such as Gabon's 1989 law, [152] Kenya's 1988 law,[153] or Sri Lanka's 1987 law.[154] Similarly, most countries of Central and Eastern Europe have also recently adopted competition laws. Some common elements and differences can be distiguished in the treatment of mergers in developing countries' competition laws in respect, *inter alia*, of market definition, the anti-competitive threshold to be attained, market share thresholds, the relative importance of structural and behavioural factors, the relative importance of risks of dominance and collusion, and the treatment of efficiency gains.

130. The Brazilian law proscribes mergers undertaken with a view to inhibiting free competition which lead to distortion in the market, as well as abuses of economic power from the control of Brazilian markets or the elimination of competition (which can arise, *inter alia* through mergers, the association of companies or interlocking directorates). A balanced efficiency defence has recently been introduced. In assessing whether there is an abuse of economic power, the competition authority considers improvements in production, distribution, efficiency, technological or economic development, and exports, as well as whether there will be an equitable distribution of the resultant profits between producers and consumers, whether the limits strictly necessary to ensure the attainment of these objectives are not exceeded, and whether competition will not be eliminated from a substantial part of the market. Even if these conditions are not met, the authorities may approve an agreement or economic concentration when it is necessary for predominant reasons relating to the national economy and the common good, when it is of a predetermined duration and when, without its implementation, the consumer or end-user could suffer prejudice.

131. In India, mergers or amalgamations involving, or which would result in, the creation of an undertaking possessing a certain asset worth, or a "dominant undertaking" (holding 25 per cet market share of an item in India or a substantial part thereof) of a lower asset worth, require permission from the Government, which can refer the merger to the MRTP Commission to assess whether it would lead to a concentration of economic power to the common detriment. Asset worth or market dominance are assessed, in appropriate cases, with reference to membership in a group of "interconnected undertakings", linked by common or interlocking ownership, control or

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147 Such countries include Argentina, Brazil, Chile, Côte d'Ivoire, Gabon, Kenya, India, Pakistan, Peru, Republic of Korea, Sri Lanka, Thailand and Venezuela. Several other countries are considering the adoption of competition laws.

148 Law No. 4137 of 10 September 1962 concerning the suppression of abuses of economic power. See also Decree No. 52025 of 20 May 1963 containing the regulations given effect to the law.

149 See Act No. 8158 of 8 January 1991, instituting provisions for the protection of competition and other measures.

150 The Monopolies and Restrictive Trade Practices Act 1969.

151 The Monopolies and Restrictive Trade Practices (Control and Prevention) Ordinance 1971.

152 Loi No. 5/89 on competition of 6 July 1989.

153 The Restrictive Trade Practices, Monopolies and Price Control Act 1988.

154 The Fair Trading Commission Act, No. 1 of 1987.

management. However, mergers among interconnected undertakings are exempted. In exercising their power, the Government or the Commission take into account the general economic position of the country, including *inter alia* efficient production, supply, distribution and trade in home and overseas markets; allocative efficiency; technical improvements in trade and market expansion; and encouragement of countervailing market power. Recently, however, there has been a substantial liberalization of Indian competition law.

132. Similar attention is paid to "associated undertakings" in Pakistan: the creation or maintenance of any relationship between competing firms having at least one-third market share between them which provides one of the owners or partners with at least one-third control of the other firm constitutes "unreasonable monopoly power". Such power can also arise where an acquisition or merger is likely to create monopoly power or to substantially lessen competition in any market. However, the Pakistani law provides for a balancing of any monopoly power created against any efficiencies arising in production, distribution, services, technical progress or exportation, if these could not have been achieved by less anti-competitive means and if they clearly outweigh the absence or lessening of competition.

133. A similar balancing test is applied in Sri Lanka. There is a general prohibition against mergers exceeding a prescribed market share or giving rise to control or dominance of the market (attention is again paid to interconnected bodies), but a merger may be authorized if it is not likely to operate against the public interest, using criteria similar to those used in the United Kingdom law. Similarly, in Kenya, a merger may be permitted if it will lead to efficiencies resulting in better competitiveness vis-à-vis imports or in export trade, thereby increasing employment, but account will also be taken of whether it reduces competition in domestic markets, increases the ability of oligopolistic producers to manipulate domestic prices, or encourages capital-intensive rather than labour-intensive technology. In Kenya, only horizontal mergers are controlled (as in some other developing countries), but existing vertical concentration of economic power may be investigated.

134. In the Republic of Korea the competition law aims at stimulating creative business activities and innovation, protecting consumers and promoting a balanced development of the national economy.[155] To this end, it *inter alia* restricts business integration, prohibits investment holdings and cross-investments among parent and subsidiary firms and limits the equity investments of big business groups (conglomerate concentration has not so far been controlled, but will be covered in future). Cross-holdings among subsidiaries cannot exceed 40 per cent. "Business integration" by firms whose equity capital or assets exceed around $1.5 or $7 million respectively is restricted if the firm may cause substantial injury to competition in any line of commerce. Exceptions may be made for "business integration" aimed at rationalization or strengthening of the international competitiveness of the relevant industry.

135. Out of the 1,846 cases of "business integration" reported up to 1989, the Fair Trade Commission of the Republic of Korea issued 293 warnings for correction, two recommendations for correction, and seven orders to cease and desist. An example of how the balancing of efficiency/competitiveness and competition has been undertaken by the Commission is provided by the case of Dong Yang Chemical Industries Co. Ltd., involving a proposed merger of two competitors respectively holding 54 and 19 per cent of the PVC stabilizer market. In that case, arguments relating to the reduction of production costs through technology exchange, reduction of transportation and packing costs, possibilities for raising export prices, avoidance of overlapping in R and D, and existence of competition from imports and substitute products, were found unconvincing by the Fair Trade Commission, which considered that the merged firm would be able to abuse a monopoly and that price rises in exports could be achieved by refraining from excessive competition through dumping.[156]

136. A number of issues or problems have arisen in different countries in the implementation of competition law.[157] A fundamental question has been the appropriate balance between ensuring more competition and achieving greater economic efficiency. This has manifested itself not only at the level of individual cases but in general government policy. Indeed the two are interrelated,

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155 See Monopoly and Fair Trade Act, Law No. 3320 of 31 December 1980 (as amended), Art. 1.

156 Corrective Order No. 82.1, 13 January 1982, EPB, the MRFT Act Decision 153 (1982).

157 See "Control in India of restrictive business practices", (UNCTAD/ST/MD/20), consultant study prepared by Mr. H.K. Paranjape; "Corporate Behaviour in restraint of trade of goods and services in Pakistan"; and "Asian Regional Seminar on Restrictive Business Practices: Report of the Course Director" (UNCTAD/RBP/TA/2).

since the latter sets the framework for the former; ambiguities in government policy and lack of clear guidelines have hampered decision-making in competition cases. Moreover, in some countries, where it is the responsibility of government ministries to refer individual cases to competition authorities, efficiency considerations, as well as political factors, have prevented such referrals (despite the fact that the evaluation procedures of competition authorities could well take efficiency considerations into account).

137. It would appear advisable for developing countries to squarely address the convergence and the potential tensions between competition and efficiency goals, as well as links between firm-level and macro-economic efficiency, the extent to which efficiencies would have to be passed on to the consumer or could be retained as producer surplus, links between efficiency and competitiveness, and the burden of proof regarding efficiences. In this connection, the solutions adopted by the new Brazilian law (see paragraph 130 above) may serve as a useful guide. In practice, of course, tensions between competition and efficiency are always likely to persist; as noted in the preceding section, some developed countries, despite their experience in the application of competition law, are still facing such problems. Yet the adoption of clear and consistent policies by developing countries, tailored to suit the competitive conditions in their markets, yet taking into account the increasing exposure of these markets and their national firms to international competition, would do much to ease the task of their competition authorities.

138. Another problem has been the lack of public and business awareness of what competition entails. In some countries, collusion and other restrictive business practices have become entrenched business habits. Moreover, in dealings with foreign suppliers using restrictive business practices, those primarily affected do not even realise what is going on, or do not know that there are recourse procedures available.[158] Painstaking pedagogical efforts have been made to correct this situation in countries such as Chile. The detection of RBPs and effective application of competition law in developing countries clearly depends to a large extent upon such pedagogical efforts. Thus, for an RBP authority to function effectively, it has been found that it has to be known and trusted by the public at large.

139. Evidence-gathering is another key issue. Problems in different countries have included: difficulties in delineating the relevant market, market shares and company assets in the absence of available, reliable, or disaggregated economic or product data or company accounts, and of enough staff with the requisite skills; difficulties in proving that firms are really interconnected; and insufficient investigatory powers. The proposed adoption of a pre-notification system for mergers in Sri Lanka is an example that might be considered in this connection. A related question is allowing private recourse to the courts in competition cases. This is allowed in Kenya, for instance, but misgivings have been expressed about possible misuse of this right by competitors.[159] Enforcement problems have also been experienced with appeals to the courts, arising principally from delays and from judicial misunderstanding of the reasoning applied.

140. As regards agreements originating from overseas, the law has been applied to local firms and TNC subsidiaries alike in appropriate cases, but little attempt has been made to exercise extraterritorial jurisdiction. Thus, the Indian competition law provides that, where a monopolistic or restrictive trade practice is carried out by a party not carrying on business in India, an order may be made with respect to that part of the practice carried on in India. This has been enforced in appropriate cases (see para. 40 above). The competition law in one Asian country has been enforced in cases, where, for example, a contract has been entered into overseas for the supply of imported dried fruit, excluding other importers from importing the fruit from the exporting country in question.[160] However, there is little evidence that competition law has been applied in respect of mergers originating from overseas. In the Pakistani case mentioned in paragraph 79 above, it is noteworthy that it was some years after the overseas merger had occurred that the competition authorities found out about it, were able to link it to the rise in tea prices, and eventually to make a limited divestment order in respect of one of the local subsidiaries. Preventive action would obviously have been preferable.

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158 See W. Latapiat, "Preventing collusion and abuse of dominant positions: the experience of Chile", in *Symposium on Competition and Economic Development*, OECD, October 1989.

159 See S. Wainaina, "Means of Competition Law Enforcement", in *Symposium on Competition and Economic Development*.

160 See "Asian Regional Seminar".

141. It is likely that wider adoption and more effective implementation by developing countries of competition laws will affect local TNC subsidiaries more often and will also start to lead to more attempts to obtain information about overseas arrangements of TNCs from Governments of developed countries, from TNC parent companies or affiliates in other countries and from other parties overseas (given the stronger impact that overseas acquisitions of control should have upon developing countries which have liberalized their trade and investment régimes). Any widespread adoption of pre-notification systems would clearly pose difficult practical problems for TNCs. It would therefore appear essential that bilateral and multilateral consultations and cooperation among competition authorities of developed and developing countries be strengthened, and that developing countries should provide their contribution to any search for new avenues of cooperation.

142. However, for individual developing countries to participate in this process, it would be essential for them to adopt and/or effectively apply competition laws in general, and merger control laws in particular, as well as to ensure that such laws are up-to-date and in tune with both the specific conditions in their domestic markets and the global competition environment. Cooperation from other countries would assist the developing countries to undertake the necessary reforms. The rapidity with which new or amending legislation is being adopted does indeed indicate that, in the light of the widespread trends towards liberalization, deregulation, privatization and market orientation, Governments of developing countries are attaching increasing importance to competition policy as a means of protecting consumer interests, providing rules of the game for the functioning of markets and ensuring that the economic benefits of liberalization are not nullified by private restrictions. But great efforts continue to be necessary to enable States to adopt or modernize competition laws, including merger controls, to apply them effectively and to undertake the necessary pedagogical endeavours to raise consciousness of competition issues at the national level. In the application of such laws, attention to changes in market structure arising, *inter alia*, through mergers is particularly important during the present period of transition towards more market-oriented economies, as such changes may well have a lasting impact, positive or negative, upon the success of such liberalization.

C. International cooperation

143. A number of bilateral and plurilateral cooperation agreements dealing with competition have been entered into by developed countries. The United States Government has entered into agreements with the governments of Australia, Canada and Germany and with the European Commission. Germany also has an agreement with France. The OECD has also dealt with the subject.[161] With variations, these agreements usually provide for notification or requests for initiation of investigations affecting important interests of other countries party to the agreement, the supply of relevant information, the taking into account of the other parties' significant interests when investigating or applying remedies, and coordinated action in respect of the same anti-competitive agreement. The United States/European Commission agreement provides, as well, for a number of factors to be taken into account in seeking to accommodate competing interests. The notification and consultation parts of these agreements appear to be working well. However, information exchange has been hampered by questions of confidentiality. In any event competition authorities would often have no knowledge of transactions having effects solely outside the country. The conciliation mechanism provided for by the OECD resolution has never been used.

144. Regional economic integration trends are also having an impact upon cooperation agreements. Thus, the EEC and EFTA countries, in the context of their agreement for the creation of a European Economic Area, have agreed on the creation of an EFTA competition authority which would apply the same rules as EEC competition law and enforcement policy (due to legal difficulties, the agreement is not yet in force). Czechoslovakia, Hungary and Poland have also

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[161] The latest OECD resolution is the Revised Recommendation of the Council concerning cooperation between members countries on RBPs affecting international trade of 21 May 1986.

agreed, in trade and co-operation agreements with the EEC, to adopt and apply the EEC competition approach. The negotiations on the North American Free Trade Agreement (NAFTA) are reported to be considering modalities for strengthening co-operation on competition.

145. At the multilateral level, no cooperation mechanisms exist to date beyond those provided for in the RBPs Set. Sir Leon Brittan, in the context of his suggestions relating to a link between competition and the international trading system (see paragraph 100 above), has suggested, in relation to cartels, that a clear line be drawn between acceptable industrial co-operation and unacceptable restrictive practices; Governments would have to show that they had used their endeavours to prevent or punish them. On mergers, he has accepted that common rules on their appraisal should be drawn up, and international panels be established to provide a forum for discussion of individual merger cases which involve several jurisdictions, and to undertake an impartial analysis of their merits and of which authority is best placed to deal with them.

146. It is arguable that such measures are premature (at least in respect of mergers), given that cases involving overlapping jurisdictional claims have been relatively few compared to the total volume of cases dealt with by competition authorities, and that such cases have been smoothly handled in accordance with established procedures, jurisdictional doctrines and comity considerations and in consultation with other competition authorities where appropriate; the sharp controversies which arose in the past have greatly diminished. However, difficulties which are already arising will undoubtedly increase in the future. It is clear that, in a world where markets have become interdependent, where enterprise transactions increasingly cross national borders, and where more competition laws are being adopted and effectively implemented, more and more Governments will seek to claim concurrent jurisdiction over a single transaction. As their competition analyses and interests (including interests relating to the promotion of competitiveness through acquisitions of control) would be based upon effects upon their national markets or, possibly, their export trade, their reactions may well diverge, possibly leading to controversy. Such a climate would hardly enhance security and predictability for enterprises and in any event, enterprises are likely to be faced with difficulties in coping with the procedural requirements of different competition authorities.

147. Since comity is considered in most countries to be a non-legal and discretionary standard, not preventing States from exercising legal jurisdiction whenever their own interests are materially affected, it cannot by itself suffice to prevent conflicts. Nor can other legal or enforcement principles, for the reasons noted above. Moreover, existing co-operation procedures do not appear to be sufficient to enable Governments to build a consensus over individual cases. Comity and official co-operation would also hardly deter the initiation of private suits. Nor can comity suffice to meet the challenges arising from the globalisation of the world economy, which may require more positive cooperation and co-ordination to obtain evidence, to deal with dangers of international oligopolisation in some industries, to defuse trade tensions and to avoid risks that national enforcement efforts will be deterred by concerns about less stringent enforcement in other countries putting national enterprises at a disadvantage when competing in international trade (see paragraph 100 above). Bilateral, regional or plurilateral co-operation, while useful, cannot suffice by themselves to cope with such tasks.

148. It may therefore be prudent for competition authorities to undertake a dialogue, in a multilateral forum, on the appropriateness of, and modalities for progressive strengthening of co-operation mechanisms for dealing with such questions, so as not to be obliged to react in an *ad hoc*, hasty and uncoordinated manner when problems arise. The consultation machinery provided for under the RBPs Set would be well suited for such informal exploratory discussions.